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No.

# In the Supreme Court of the United States

JAVIER RIVERA AQUINO, SECRETARY,
PUERTO RICO DEPARTMENT OF AGRICULTURE,
ET AL., PETITIONERS

*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTION PRESENTED

Whether a federal court can order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury.

## PARTIES TO THE PROCEEDING

Petitioners are Javier Rivera Aquino, Secretary of the Puerto Rico Department of Agriculture, and Cyndia E. Irizarry, Administrator of the Puerto Rico Milk Industry Regulatory Administration. Respondents are Suiza Dairy, Inc., and Vaquería Tres Monjitas, Inc.

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## PETITION FOR A WRIT OF CERTIORARI

Javier Rivera Aquino, Secretary of the Puerto Rico Department of Agriculture, and Cyndia E. Irizarry, Administrator of the Puerto Rico Milk Industry Regulatory Administration, respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the First Circuit in this case.

### OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-44a) is reported at 587 F.3d 464. The court of appeals' order denying rehearing (App., *infra*, 45a-68a) is reported at 600 F.3d 1. The district court's order denying petitioners' motion to dismiss (App., *infra*, 199a-218a)

and its order granting respondents' motion for preliminary injunction (App., *infra*, 69a-198a) are unreported.

## JURISDICTION

The judgment of the court of appeals was entered on November 23, 2009. A petition for rehearing was denied on March 11, 2010 (App., *infra*, 45a-68a). On June 2, 2010, Justice Breyer extended the time within which to file a petition for a writ of certiorari to and including July 9, 2010. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

## STATEMENT

1. This case presents a question of sovereign immunity arising out of litigation concerning the Puerto Rico milk industry. In Puerto Rico, as in many States, the milk industry is regulated in order to ensure a consistent supply and stable prices for consumers and producers. Pursuant to statute, the primary regulatory agency is the Puerto Rico Milk Industry Regulation Administration (Oficina de Reglamentación de la Industria Lecheria or ORIL), a subdivision of the Puerto Rico Department of Agriculture. For many decades, ORIL has set both the minimum price at which fresh milk processors buy raw milk from dairy farmers and the maximum price at which those processors sell fresh milk to the public. App., *infra*, 5a.

There are three processors of milk in Puerto Rico: respondent Suiza Dairy, Inc. (Suiza); respondent Vaquería Tres Monjitas, Inc. (Tres Monjitas); and Industria Lechera de Puerto Rico, Inc. (Indulac). Suiza and Tres Monjitas buy raw milk and process it into fresh milk; they are the only sellers of fresh milk in Puerto Rico. Indulac buys surplus raw milk and, *inter alia*, processes it into ultra-high-temperature (UHT) milk, a type of milk that does not require refrigeration. Indulac

controls a majority of the market for UHT milk; the rest originates outside Puerto Rico. Although ORIL historically did not set the maximum price at which UHT milk was sold to the public, UHT milk was less expensive than, and thus gained market share relative to, fresh milk. App., *infra*, 5a-7a.

2. Petitioners are the Secretary of the Puerto Rico Department of Agriculture and the Administrator of ORIL. On August 13, 2004, respondents filed suit in the United States District Court for the District of Puerto Rico against, *inter alios*, petitioners in their official capacities. Respondents alleged that, by depriving them of a reasonable rate of return and favoring UHT milk produced by Indulac, Puerto Rico's regulatory scheme violated the Takings, Due Process, Equal Protection, and Commerce Clauses of the federal Constitution. App., *infra*, 11a. In the operative version of their complaint, respondents sought not only an injunction against continued enforcement of the regulatory scheme, but also the creation of a "temporary mechanism for [respondents] to recover the losses they have experienced on account of the unconstitutional acts and decisions herein under attack." Second Am. Compl. ¶ 92, at 39. Shortly after filing the complaint, respondents moved for a preliminary injunction. App., *infra*, 11a.

Petitioners moved to dismiss the complaint, raising a variety of defenses including sovereign immunity. The district court denied the motion. App., *infra*, 202a-221a. As is relevant here, the court reasoned that, "[i]n the instant case, [respondents] are seeking a prospective injunctive relief against [petitioners] to avoid insolvency[,] but they are not seeking damages nor a monetary compensation." *Id.* at 217a.

After more than fifty evidentiary hearings, the district court issued an order granting respondents' motion

for preliminary injunction. App., *infra*, 69a-198a. The court held that respondents not only were likely to succeed on their constitutional claims, but had in fact shown that they had suffered a past and ongoing "Due Process and Equal Protection violation reaching levels of a 'taking.'" *Id.* at 192a. After weighing the equities, the court determined that respondents were entitled to a preliminary injunction. *Id.* at 192a-194a. The court ordered the Administrator of ORIL not only to revise the regulatory scheme so as to allow respondents to recover a higher rate of return going forward, but also to "adopt a temporary mechanism that will allow [respondents] to recover the new rate of return * * * for the year 2003 * * * and up to the day when they begin to recover said rate." *Id.* at 197a. With regard to the latter remedy, the court provided that "[t]he Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of [the Administrator's] choosing." *Ibid.*

In compliance with the district court's order, the Administrator of ORIL promulgated a regulation and accompanying administrative order imposing a 1.5¢ surcharge on every quart of milk sold in Puerto Rico for the purpose of compensating respondents for their lost revenues. App., *infra*, 22a & n.17. The proceeds from the surcharge were to have been held in a segregated account by the Milk Industry Development Fund; in fact, some of the proceeds have been directly retained by respondents. *Id.* at 22a; Pet. D. Ct. Opp. to Mot. for Contempt 6-7.

3. Petitioners appealed the district court's order, contending, *inter alia*, that, by ordering retrospective monetary relief, the district court had violated Puerto Rico's sovereign immunity. The court of appeals affirmed. App., *infra*, 1a-44a.

As is relevant here, the court of appeals rejected petitioners' sovereign-immunity challenge. App., *infra*, 22a-28a. The court expressly declined to address whether the relief ordered was prospective or retrospective. *Id.* at 24a. Instead, the court asserted that "the source of relief [was] of paramount importance" to the sovereign-immunity inquiry. *Id.* at 25a. Focusing on that consideration, the court noted that "none of the compensation would come from the [Commonwealth's] treasury," *id.* at 24a, because "the money in question would come directly from consumers of milk in Puerto Rico" and "would be neither collected by government entities nor retained in the Commonwealth's treasury." *Id.* at 26a. On that basis, the court held that sovereign immunity "does not bar the form of relief granted by the district court." *Id.* at 28a.

4. Petitioners filed a petition for rehearing en banc. Over a lengthy dissent by Chief Judge Lynch, the court of appeals denied the petition. App., *infra*, 45a-68a.

a. In her dissent, Chief Judge Lynch stated that "the serious issues raised deserve greater attention from this Court and, failing that, from the Supreme Court." App., *infra*, 54a. She reasoned that, by upholding the district court's order simply because it "did not force the Commonwealth to satisfy the judgment with funds directly paid from or funneled through [its] treasury," *id.* at 55a, the panel's decision was "inconsistent with more than a decade's worth of * * * Supreme Court precedents," as well as "precedent from other circuits." *Id.* at 55a-56a.

Chief Judge Lynch explained that "[t]here can be no doubt that the injunction at issue makes the Commonwealth, through one of its administrative agencies, liable for retrospective monetary relief": specifically, by "allow[ing] [respondents] to recover the *past* profits they

say they lost between 2003 and the time of the injunction." App., *infra*, 60a, 61a. In her view, the panel "most likely depart[ed] from precedent when it h[eld] that [sovereign immunity] is not involved when the Commonwealth is ordered to raise money from individuals through mechanisms other than a general tax that produces funds for [its] treasury." *Id.* at 62a-63a. Such an approach, she continued, would "provide[] an easy mechanism for evasion" of sovereign immunity, *id.* at 63a, and "elevate[] form over substantive reality," *id.* at 66a.

Instead, Chief Judge Lynch reasoned, "[w]hen a state raises revenues through the methods available to it as a sovereign—including taxation and regulatory orders—rather than by withdrawing existing funds in the state treasury, this surely does not remove the Eleventh Amendment's protections." App., *infra*, 64a. "Either way," she explained, "the state fisc is affected because the state is being required to use its own resources to replace the original source of the plaintiffs' profits." *Ibid.* (internal quotation marks omitted). Chief Judge Lynch concluded that, "[i]f courts can evade Eleventh Amendment constraints by dictating to states that they find ways in which state officials can use the state's regulatory money-raising powers to satisfy a money judgment, the Eleventh Amendment's bar against retrospective monetary relief becomes a nullity." *Id.* at 67a-68a.

b. Judge Torruella, who had written the panel opinion, concurred in the denial of rehearing en banc. App., *infra*, 46a-54a. He contended that the panel's decision was "eminently correct" because "well-established precedent * * * places decisive weight on the impact a judgment has on the state treasury." *Id.* at 47a. "In this case," he continued, sovereign immunity "poses no bar to relief because there is simply no impact on the [Commonwealth's] fisc, *at present or in the future*." *Ibid.* He

further explained that "[t]he Commonwealth simply has not been required to appropriate *its funds* to comply with the regulatory accrual." *Id.* at 50a. Because "[t]his case simply does not involve a monetary award against the [Commonwealth] that burdens [its] treasury," Judge Torruella concluded that it did not implicate Puerto Rico's sovereign immunity. *Id.* at 54a.

## REASONS FOR GRANTING THE PETITION

In the decision below, the First Circuit held that a federal court could order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury. The First Circuit's decision conflicts with the decisions of other circuits on the circumstances, if any, under which retrospective monetary relief may be awarded consistent with sovereign immunity. The First Circuit's decision, moreover, cannot be reconciled with this Court's sovereign-immunity jurisprudence. And the question presented by this case is undeniably one of great importance to Puerto Rico and other sovereigns. In sum, as Chief Judge Lynch stated in her dissent from the denial of rehearing en banc, this case presents "serious issues" that "deserve [the] attention" of the Court. App., *infra*, 54a.

### A. Sovereign Immunity Generally Prohibits Suits Against Sovereigns Except For Suits Against Officials Seeking Prospective Relief

1. While it is codified in the Eleventh Amendment, the principle of sovereign immunity "derives * * * from the structure of the original Constitution itself." *Alden* v. *Maine*, 527 U.S. 706, 728 (1999).[1] In federal

[1] The lower courts in this case assumed that Puerto Rico, as a territory with substantial autonomy, is entitled to sovereign immunity.

court, that principle "limits the grant of judicial authority in Art[icle] III" by preventing sovereigns from being sued unless they have unambiguously consented to suit or Congress has expressly abrogated their immunity. *Pennhurst State Sch. & Hosp.* v. *Halderman*, 465 U.S. 89, 98 (1984). The principle of sovereign immunity protects not only sovereigns themselves, but also their officials when sued in their official capacities, because a suit against an official "is no different from a suit against the [sovereign] itself." *Will* v. *Michigan Dep't of State Police*, 491 U.S. 58, 71 (1989).

2. In *Ex parte Young*, 209 U.S. 123 (1908), this Court carved out the now-familiar exception to the principle of sovereign immunity for suits against officials to enjoin official actions that violate federal law. See *id.* at 159-160. In so doing, the Court stated that a sovereign "has no power to impart to [its official] any immunity from responsibility to the supreme authority of the United States." *Id.* at 160. The Court has since explained that the rationale for the *Ex parte Young* exception is that "[r]emedies designed to end a continuing violation of federal law are necessary to vindicate the federal interest in assuring the supremacy of that law." *Green* v. *Mansour*, 474 U.S. 64, 68 (1985).

In the century since *Ex parte Young* was decided, this Court has repeatedly made clear that its exception is

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Since its decision in *Erzatty* v. *Puerto Rico*, 648 F.2d 770, 776 n.7 (1981) (Breyer, J.), the First Circuit—the geographic circuit with jurisdiction over Puerto Rico—has so held in dozens of cases. Respondents have not disputed the proposition that Puerto Rico is entitled to sovereign immunity at any stage of this litigation, and the Court has previously decided at least one other case involving Puerto Rico on the same assumption. See *Puerto Rico Aqueduct & Sewer Auth.* v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 n.1 (1993).

available only where "[the] complaint alleges an ongoing violation of federal law and seeks relief properly characterized as prospective." *Verizon Md. Inc.* v. *Public Service Comm'n*, 535 U.S. 635, 645 (2002) (internal quotation marks and citation omitted). Accordingly, the Court has consistently rejected efforts to "extend the reasoning of [*Ex parte*] *Young* * * * to claims for retrospective relief." *Green*, 474 U.S. at 68; see *Quern* v. *Jordan*, 440 U.S. 332, 337 (1979) (confirming that "[t]he distinction between that relief permissible under the doctrine of *Ex parte Young*" and relief barred by sovereign immunity is "the difference between prospective relief on one hand and retrospective relief on the other"). The Court has justified that limitation on the reach of *Ex parte Young* on the ground that permitting retrospective relief "would effectively eliminate the constitutional immunity of the States." *Pennhurst*, 465 U.S. at 105; see *Edelman* v. *Jordan*, 415 U.S. 651, 653, 663 (1974). And the Court has urged lower courts, in engaging in that "straightforward inquiry," *Verizon*, 535 U.S. at 645, to "look to the substance rather than the form of the relief sought," *Papasan* v. *Allain*, 478 U.S. 265, 279 (1986)—and to bar claims for "[r]elief that in essence serves to compensate a party injured in the past." *Id.* at 278; see, *e.g.*, *Edelman*, 415 U.S. at 666; *Ford Motor Co.* v. *Department of Treasury*, 323 U.S. 459, 464 (1945).

3. Critically for purposes of this case, the Court has made clear that, where a plaintiff is seeking retrospective monetary relief, the defense of sovereign immunity is available regardless of the source of the funds that would be used to discharge any judgment. Most notably, in *Regents of University of California* v. *Doe*, 519 U.S. 425 (1997), the Court unanimously held that a state agency possessed sovereign immunity even though the federal government had agreed to indemnify the agency

in the event of an adverse judgment. *Id.* at 431. The Court explained that, for purposes of sovereign immunity, "it is the entity's potential legal liability, rather than its ability or inability to require a third party to reimburse it, or to discharge the liability in the first instance, that is relevant." *Ibid.*

### B. The Court Of Appeals' Decision Conflicts With The Decisions Of Other Courts Of Appeals

In the decision below, the First Circuit held that a federal court could order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury. See App., *infra*, 25a-26a. No other court of appeals has adopted such a narrow view of the doctrine of sovereign immunity since this Court's decision in *Doe*, and several other courts of appeals have held that the defense of sovereign immunity is available whenever a plaintiff is seeking retrospective monetary relief, regardless of the effect of any judgment on the sovereign's treasury. The resulting conflict warrants this Court's review.

1. Four courts of appeals—the Fifth, Seventh, Tenth, and Eleventh—have held that sovereign immunity bars any suit in which the plaintiff is seeking retrospective monetary relief. In *Esparza* v. *Valdez*, 862 F.2d 788 (1988), the Tenth Circuit specifically rejected the contention that a suit seeking retrospective monetary relief for unemployment benefits should be allowed to proceed because the funds to satisfy any judgment would have come from "a special, segregated fund as distinguished from a general revenue fund." *Id.* at 794. The court held that the proposed distinction was irrelevant because, whatever the source of the funds, "an injunction ordering retroactive benefits effectively would be an award of money damages for past violations of federal

law that is precluded" by sovereign immunity. *Ibid.* (internal quotation marks and citation omitted).[2]

Relying on *Esparza*, the Seventh Circuit reached the same conclusion in another suit seeking retrospective monetary relief for unemployment benefits. See *Paschal* v. *Jackson*, 936 F.2d 940 (1991). Like the Tenth Circuit, the Seventh Circuit expressed "great difficulty with the view that a state's fiscal structure is dispositive of whether one can sue the state for accrued benefits." *Id.* at 944. The court "disregard[ed] the source of state funds" on the ground that "[w]here [the state] gets the money to satisfy a judgment is no concern of the plaintiff or the court." *Ibid.* (citation omitted). Instead, "what matters is that the judgment runs against the state." *Ibid.* (citation omitted).

Similarly, in *Cronen* v. *Texas Department of Human Services*, 977 F.2d 934 (1992), the Fifth Circuit held that sovereign immunity barred a suit seeking retrospective monetary relief for welfare benefits. *Id.* at 938. The court reasoned that, although the benefits the plaintiff was seeking "would be paid entirely by the federal government," "the source of the damages is irrelevant when the suit is against the state itself or a state agency." *Ibid.*[3]

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[2] Since its decision in *Esparza*, the Tenth Circuit has reiterated that, in analyzing whether an entity was an arm of the State for sovereign-immunity purposes, it "focus[es] on the legal incidence * * * of the liability" and not on "the practical effect" on the sovereign's treasury. *Sturdevant* v. *Paulsen*, 218 F.3d 1160, 1165 (2000).

[3] Although the court did leave open the possibility, in dicta, that a similar claim could proceed against a state official, it did not elaborate on why the identity of the named defendant would matter as long as the suit was seeking retrospective rather than prospective relief. See *Cronen*, 977 F.2d at 938.

Finally in this category of cases, the Eleventh Circuit held that a district court violated a State's sovereign immunity in a suit in which disabled individuals initially sought injunctive relief for alleged violations of a federal statute. See *Florida Association of Rehabilitation Facilities, Inc.* v. *Florida Dep't of Health & Rehabilitative Services*, 225 F.3d 1208 (2000). The court reiterated the principle that the availability of the exception of *Ex parte Young* "turns, in the first place, on whether the plaintiff seeks retrospective or prospective relief." *Id.* at 1219. Applying that principle, the court of appeals held that, when the district court ordered state officials "to redress inequities in their *past* reimbursement payments * * * and potentially to reimburse [p]laintiffs for those past deficiencies," it violated the State's sovereign immunity. *Id.* at 1220. The court explained that "[t]he fact that harm is ongoing in the sense that [p]laintiffs are continuing to suffer the effects of [d]efendants' prior failure to reimburse them adequately does not make the relief any less retrospective." *Id.* at 1221. In addition, the court rejected the plaintiffs' contention that the outcome should be different because the federal government would provide offsetting funds and the State's treasury would therefore not be affected. *Id.* at 1225. The court reasoned that such a principle "cannot readily be squared with the Supreme Court's Eleventh Amendment jurisprudence." *Ibid.*

2. The Sixth Circuit has taken a subtly different approach, although the result of that approach is seemingly the same: *i.e.*, to bar suits in which the plaintiff is seeking retrospective monetary relief. In *Ernst* v. *Rising*, 427 F.3d 351 (2005) (en banc), the Sixth Circuit considered whether sovereign immunity barred a suit seeking retrospective monetary relief for retirement benefits. *Id.* at 354-355. In the context of analyzing whether a

state retirement system was an arm of the State for sovereign-immunity purposes, the court rejected the plaintiffs' contention that any judgment in their favor would be paid out of funds belonging to the retirement system, rather than the State's general treasury. *Id.* at 361-362. Writing for the court, Judge Sutton reasoned that the proper inquiry was not "whether the state treasury would be liable in *this* case," but rather "whether, hypothetically speaking, the state treasury would be subject to potential legal liability *if* the retirement system did not have the money to cover the judgment." *Id.* at 362 (internal quotation marks and citation omitted). As a practical matter, the Sixth Circuit's approach is not materially different from that of the other circuits discussed above, because it focuses on the legal incidence of any liability for retrospective monetary relief—and bars suit where the liability falls on the sovereign.

3. In this case, the First Circuit took a dramatically different approach, holding that a federal court could order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury. See App., *infra*, 25a-26a. That approach simply cannot be reconciled with the approaches of the circuits discussed above, which focus on the legal incidence of any liability rather than on the source of the funds used to satisfy any judgment in the plaintiff's favor.

No other court of appeals has permitted a federal court to order retrospective monetary relief against a sovereign since this Court's decision in *Doe*. Even before *Doe*, only two courts of appeals had so held. In *Brown* v. *Porcher*, 660 F.2d 1001 (1981), the Fourth Circuit held—in circumstances materially identical to the Tenth Circuit's decision in *Esparza* and the Seventh Circuit's decision in *Paschal*—that sovereign immunity did

not bar a judgment awarding retrospective monetary relief for unemployment benefits. *Id.* at 1003. In the Fourth Circuit's view, the judgment was not barred because the funds the plaintiffs were seeking were "insulated" and "separately financed" from the State's general treasury. *Id.* at 1007. Notably, although this Court ultimately denied review, three Justices dissented from the denial of certiorari. See 459 U.S. 1150 (1983) (opinion of White, J., joined by Powell and Rehnquist, JJ.). In his dissent—written even before *Doe*—Justice White explained that the distinction drawn by the Fourth Circuit was "certainly questionable under this Court's previous cases." *Id.* at 1153. He added that "whether there are some state funds that do not enjoy Eleventh Amendment immunity" was an "important" question that merited the Court's review. *Ibid.*

Similarly, the Third Circuit held—in circumstances materially identical to the Fifth Circuit's decision in *Cronen* and the Eleventh Circuit's decision in *Florida Association of Rehabilitation Facilities*—that sovereign immunity did not bar the award of retrospective monetary relief for benefits "to the extent that [the state agency] will be reimbursed by the United States." *Bennett* v. *White*, 865 F.2d 1395, 1408 (1989). Although the Third Circuit relied on that holding in a subsequent case, see *Robinson* v. *Block*, 869 F.2d 202, 214 n.11 (1989), it has not done so in any case since *Doe*.[4] Regardless of the ongoing vitality of that holding in the Third Circuit, how-

[4] To the contrary, in analyzing whether an entity was an arm of the State for sovereign-immunity purposes, the Third Circuit has noted that a "key factor" was "the potential legal liability of the Commonwealth for [the defendant's] debts" in the event the defendant were unable to pay. *Cooper* v. *Southeastern Pennsylvania Transp. Auth.*, 548 F.3d 296, 304 (2008) (citation omitted).

ever, the First Circuit's decision in this case confirms the existence of a live circuit conflict—a conflict that warrants the Court's review.

**C. The Court Of Appeals' Decision Is Erroneous**

The First Circuit erred in holding that a federal court could order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury. As Chief Judge Lynch noted in her dissent from the denial of rehearing en banc, "[t]hat is not * * * the appropriate test under the Supreme Court's Eleventh Amendment jurisprudence." App., *infra*, 55a. In fact, the First Circuit's holding is so out of step with this Court's sovereign-immunity precedents that the Court may wish to consider the possibility of summary reversal.

1. The First Circuit correctly understood that, because respondents had brought suit against Puerto Rico officials in their official capacities, the relevant question was whether respondents could invoke the exception to sovereign immunity for such suits set out in *Ex parte Young*. See App., *infra*, 23a-24a.[5] The First Circuit erred, however, when it declined to address whether the relief ordered was prospective or retrospective. *Id.* at 24a. As noted above, this Court's precedents make clear that the exception of *Ex parte Young* is available where, and only where, the plaintiff is seeking prospective relief. See pp. 8-9, *supra*.

There can be no doubt that the relief which the plaintiffs in this case were seeking, and which the district

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[5] Respondent Suiza conceded below that respondents were pursuing "an *Ex [p]arte Young* type of action" and that the exception to sovereign immunity set out in *Ex parte Young* was "[t]he exception that mainly concerns us here." Suiza C.A. Br. 35.

court ordered, was retrospective in nature. In the operative version of their complaint, respondents specifically sought to "recover the losses they have experienced on account of the unconstitutional acts and decisions herein under attack." Second Am. Compl. ¶ 92, at 39. And in the order under review, the district court ordered ORIL to compensate respondents for lost profits from the beginning of 2003—*i.e.*, more than eighteen months before respondents filed suit—to the date on which ORIL ultimately adopts a revised regulatory scheme. See App., *infra*, 197a. Although respondents contended below that the relief was prospective on the ground that its purpose was to "rebuild their capital bases," *id.* at 24a, that contention could almost always be made when a court awards retrospective monetary relief, as Chief Judge Lynch noted in dissent. See *id.* at 60a n.8. And this Court has previously expressed its disapproval of efforts to relabel as prospective what is functionally retrospective relief. See, *e.g.*, *Papasan*, 478 U.S. at 278 (noting that sovereign immunity is triggered "if the relief is tantamount to an award of damages for a past violation of federal law, even though styled as something else").

2. The First Circuit fundamentally erred, moreover, when it proceeded to hold that, even assuming that the relief at issue was properly characterized as retrospective monetary relief, a federal court could order such relief against a sovereign as long as the necessary funds do not come directly from the general treasury. See App., *infra*, 25a-26a. Since its decision in *Green*, *supra*, this Court has consistently held that, in determining whether the relief at issue is impermissibly retrospective for purposes of *Ex parte Young*, a court should not consider whether the relief has an effect on the sovereign's treasury. Most notably, in *Doe*, the Court specifically held that, where a plaintiff is seeking retrospective monetary

relief, the source of the funds that would be used to discharge any judgment is irrelevant for purposes of sovereign immunity. See 519 U.S. at 431. Instead, the Court made clear that the appropriate inquiry focuses on "the entity's potential legal liability"—*i.e.*, the legal *incidence* of any liability—"rather than its ability or inability to require a third party to reimburse it." *Ibid.*

In this case, there can be no doubt that the liability for retrospective monetary relief falls on the Commonwealth, regardless of how it comes up with the necessary funds. In the operative version of their complaint, respondents specifically sought to "recover [their] losses" from ORIL. Second Am. Compl. ¶ 92, at 39. And in the order under review, the district court directed ORIL to compensate respondents—even if the court "did not force the Commonwealth to satisfy the judgment with funds directly paid from or funneled through [its] treasury," App., *infra*, 55a (Lynch, C.J., dissenting from denial of rehearing en banc), but instead allowed ORIL to raise the funds "through * * * any * * * available mechanism of [the Administrator's] choosing," *id.* at 197a.

As Chief Judge Lynch noted in dissent, if ORIL had been unable to raise sufficient funds to compensate respondents from the surcharge it imposed, it would have been obligated to find another means of doing so. See App., *infra*, 64a. Just as the defendant in *Doe* could not be sued for retrospective monetary relief simply because it had taken steps *ex ante* to limit its exposure by means of an indemnification agreement, so too petitioners cannot be sued here simply because ORIL took steps *ex post* to limit its exposure by means of a revenue-raising surcharge. Cf. *Doe*, 519 U.S. at 431 (noting that "[s]urely if the sovereign State of California should buy insurance to protect itself against potential tort liability * * * it

would not cease to be 'one of the United States'"). In short, this case is indistinguishable from *Doe*. The First Circuit clearly erred by extending *Ex parte Young* to permit a claim for retrospective relief and holding that the district court's order awarding retrospective relief did not violate Puerto Rico's sovereign immunity.

3. In rejecting petitioners' sovereign-immunity defense, the First Circuit heavily relied on decisions in which this Court has considered whether an entity constitutes an arm of the State (and is therefore entitled to invoke the State's sovereign immunity). See, *e.g.*, App., *infra*, 25a-26a (citing *Hess* v. *Port Authority Trans-Hudson Corp.*, 513 U.S. 30 (1994)). As a preliminary matter, those cases are inapposite here for the simple reason that respondents brought suit against Puerto Rico officials in their official capacities—not against any particular entity. Even if respondents had brought suit directly against the Puerto Rico Department of Agriculture or ORIL, however, each of those entities would "clearly" qualify as an arm of the State. *Id.* at 60a (Lynch, C.J., dissenting from denial of rehearing en banc). Like its federal counterpart, the Department of Agriculture is a full-fledged department of the executive branch, see P.R. Const. Art. IV, § 6, and ORIL is a subdivision of that department, see P.R. Laws Ann. tit. 5, § 1093 (2009).[6]

But in any event, this Court's cases involving the arm-of-the-State doctrine do not support the court of appeals' holding. To be sure, in those cases, this Court ex-

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[6] Notably, in arguing before the court of appeals that the district court's order did not violate sovereign immunity, respondent Suiza assumed, *arguendo*, that ORIL was an arm of the State. See Suiza C.A. Br. 33 n.22.

plained that, in determining whether an entity is an arm of the State, a court should give substantial weight to the effect of any judgment on the State's treasury. See, *e.g.*, *Hess*, 513 U.S. at 48. In *Doe*, however, this Court made clear that, in assessing that factor in the arm-of-the-State inquiry (as in determining more generally whether sovereign immunity is available), a court should focus on the legal incidence of the liability, not on the source of the funds that would be used to discharge it. See 519 U.S. at 431; see *id.* at 430 (citing *Hess* for the proposition that "the question whether a money judgment against a state instrumentality or official would be *enforceable* against the State is of considerable importance to any evaluation of the relationship between the State and the entity or individual being sued") (emphasis added). Because there can be no doubt here that the district court awarded retrospective monetary relief or that the legal incidence of that liability falls on the Commonwealth, the First Circuit's decision cannot be reconciled with this Court's precedents. The Court should either grant plenary review or reverse outright to correct the First Circuit's seriously flawed approach.

### D. The Question Presented Is An Exceptionally Important One That Merits The Court's Review

Finally, the question presented in this case warrants the Court's review. The Court has long recognized the central importance of the doctrine of sovereign immunity as a means of protecting the power and dignity of sovereigns in our constitutional structure. See, *e.g.*, *Alden*, 527 U.S. at 715 (noting that "[t]he generation that designed and adopted our federal system considered immunity from private suits central to sovereign dignity"). Accordingly, the Court has granted review in recent years in numerous cases involving various aspects of so-

vereign immunity—including twice already in cases to be heard this Term. See, *e.g.*, *Virginia Office for Protection & Advocacy* v. *Reinhard*, cert. granted, No. 09-529 (June 21, 2010); *Sossamon* v. *Texas*, cert. granted, No. 08-1438 (May 24, 2010).

If allowed to stand, the First Circuit's decision will substantially undermine the vitality of this foundational principle of constitutional structure. The decision below allows a federal court to award retrospective monetary relief against any sovereign as long as the necessary funds do not come directly from the sovereign's general treasury. As Chief Judge Lynch noted in her dissent from the denial of rehearing en banc, that holding "provides an easy mechanism for evasion" of sovereign immunity, because a court need only direct a sovereign to generate the funds necessary to satisfy its liability by means of a tax in order to circumvent the traditional prohibition on retrospective relief. App., *infra*, 63a.

Indeed, under the First Circuit's approach, it will be impossible for sovereigns to seek dismissal of claims seeking retrospective monetary relief, because of the potential that a court will craft its relief in such a way as to avoid taking funds directly from the sovereign's general treasury. See, *e.g.*, *Federal Maritime Comm'n* v. *South Carolina Ports Auth.*, 535 U.S. 743, 765 (2002) (noting that "[s]overeign immunity does not merely constitute a defense to monetary liability or even to all types of liability" but instead "provides an immunity from suit"). If allowed to stand, therefore, the First Circuit's decision will enable plaintiffs to use *Ex parte Young* to seek retrospective as well as prospective relief—and thereby "effectively eliminate the constitutional immunity" of Puerto Rico and other sovereigns. *Pennhurst*, 465 U.S. at 105; see App., *infra*, 68a (Lynch, C.J., dissenting from denial of rehearing en banc) (noting that, under the First

Circuit's approach, "the Eleventh Amendment's bar against retrospective monetary relief [will] become[] a nullity").

Given "[the] stakes for the states in the many cases in which individuals seek compensation for past constitutional violations," Chief Judge Lynch correctly noted that this case presents "serious issues" that "deserve [the] attention" of the Court. App., *infra*, 54a, 56a (opinion dissenting from denial of rehearing en banc). The First Circuit's decision in this case authorizes the imposition on Puerto Rico of substantial monetary liability for past constitutional violations.[7] That decision is of enormous practical and conceptual importance to the Commonwealth of Puerto Rico. And it will have profound consequences for other sovereigns confronted in the future with similar claims. As explained above, the First Circuit's decision conflicts with the decisions of other circuits and cannot be reconciled with this Court's decisions. The Court should grant review and reaffirm the core constitutional principle that a sovereign may not be sued for retrospective monetary relief.

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[7] Respondents lost more than $10 million, allegedly as a result of Puerto Rico's regulatory scheme, in 2003 alone. See App., *infra*, 10a n.10.

## CONCLUSION

The petition for a writ of certiorari should be granted. The Court may wish to consider summarily reversing the judgment of the court of appeals; in the alternative, the Court should set the case for briefing and oral argument.

Respectfully submitted.

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JULY 2010

# APPENDIX

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## APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

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No. 07-2240

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VAQUERÍA TRES MONJITAS, INC.; SUIZA DAIRY, INC., Plaintiffs, Appellees,

*v.*

CYNDIA E. IRIZARRY, in her official capacity as Administrator of the Office of the Milk Industry Regulatory Administration for the Commonwealth of Puerto Rico, Defendant, Appellant,

JOSÉ O. FABRE-LABOY, in his official capacity as Secretary of the Department of Agriculture of the Commonwealth of Puerto Rico; INDUSTRIA LECHERA DE PUERTO RICO, INC. (INDULAC), PUERTO RICO DAIRY FARMERS ASSOCIATION, Defendants.

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No. 07-2369

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VAQUERÍA TRES MONJITAS, INC.; SUIZA DAIRY, INC., Plaintiffs, Appellees,

*v.*

JAIME RIVERA-AQUINO, in his official capacity as Secretary of the Department of Agriculture of the Commonwealth of Puerto Rico; Defendant, Appellant,

INDUSTRIA LECHERA DE PUERTO RICO, INC. (INDULAC); PUERTO RICO DAIRY FARMERS ASSOCIATION; CYNDIA E. IRIZARRY, in her official capacity as Administrator of the Office of the Milk Industry Regulatory Administration for the Commonwealth of Puerto Rico, Defendants.

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November 23, 2009

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Before: TORRUELLA, LIPEZ, and HOWARD, Circuit Judges.

TORRUELLA, Circuit Judge. This is an appeal from a preliminary injunction issued by the United States District Court for the District of Puerto Rico against the Milk Industry Regulation Administration for the Commonwealth of Puerto Rico ("ORIL" by its Spanish acronym), a sub-entity of the Department of Agriculture charged with regulating Puerto Rico's milk industry, and the Commissioners thereof. Plaintiffs, fresh milk processors in the Commonwealth, filed suit in federal court under 42 U.S.C. § 1983 and the Federal Declaratory Judgment Act, 28 U.S.C. § 2201, alleging that ORIL's regulatory scheme governing milk prices violates the Due Process, Equal Protection, Takings, and dormant Commerce Clauses, and seeking an order pursuant to Fed. R. Civ. P. 65(a) enjoining the Administrator of ORIL from continuing to implement the challenged regulatory provisions. Finding a likelihood of success on the merits of

plaintiffs' constitutional claims, the district court preliminarily enjoined the regulatory scheme.

On appeal, in addition to challenging the merits of the district court's preliminary injunction ruling, Defendants-Appellants argue that the district court's actions were barred by the *Burford* abstention doctrine, the Eleventh Amendment, and by various equitable defenses.

After careful consideration, we affirm.

## I. Background

### A. Factual Background[1]

#### 1. Parties

Plaintiffs-Appellees Vaquería Tres Monjitas ("Tres Monjitas") and Suiza Dairy, Inc. ("Suiza") are fresh milk processors in the Commonwealth of Puerto Rico (collectively "the processors"). Their business consists of purchasing raw milk from local dairy farmers and converting it into drinkable fresh milk, which they then sell to consumers. Plaintiffs are the only fresh milk processors in Puerto Rico. Tres Monjitas holds a market share of 34.7%, and Suiza holds a 65.3% share. As milk processors, plaintiffs fall under Puerto Rico's regulatory structure for milk and milk products.

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[1] These facts are drawn from the findings made by the district court as set forth in its amended opinion and order granting preliminary injunction after fifty-one days of hearings between February 2005 and August 2006. Defendants do not challenge the district court's factual determinations on appeal. *Vaquería Tres Monjitas, Inc.* v. *Fabre Laboy*, No. 04-1840, slip op. at 7-44 (D.P.R. July 13, 2007).

Defendant-Appellant Cyndia E. Irizarry[2] ("Administrator") is being sued in her official capacity as the current Administrator of ORIL, which is the entity responsible for creating and administering the Commonwealth's milk regulatory structure. ORIL is a subdivision of the Commonwealth's Department of Agriculture, whose current Secretary, Jaime Rivera-Aquino,[3] is also a named defendant in his official capacity.

Defendant Industria Lechera de Puerto Rico, Inc. ("Indulac") was joined to the litigation after its inception. Indulac is owned and operated by Fondo de Fomento de la Industrial Lechera ("FFIL" or "the Fund"), an entity created pursuant to the Milk Industry Regulation Act, Act No. 34 of June 11, 1957 ("Act 34") to promote Puerto Rico's milk industry. 5 P.R. Laws Ann. §§ 1092-1125 (2005 & Supp. 2008). Indulac is the sole entity in Puerto Rico authorized to process ultra high temperature milk ("UHT milk"), a type of milk that does not require refrigeration prior to opening and competes directly with the fresh milk produced by Tres Monjitas and Suiza.

The Administrator of ORIL, who is statutorily empowered to regulate the milk market, is also chairman of the board of FFIL, the government entity which owns Indulac. 5 P.R. Laws Ann. § 1099(e) (2005 & Supp. 2008). Until the milk processors filed this suit, then-serving ORIL Administrator Pedro-Gordian also chaired the Indulac board. The CEOs of ORIL and FFIL are both

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[2] Previous pleadings refer to Juan R. Pedro-Gordian, who was the Administrator at the time when they were filed. "[W]hen officials sued in [their official] capacity in federal court die or leave office, their successors automatically assume roles in the litigation." *Hafer* v. *Melo*, 502 U.S. 21, 25 (1991); *see* Fed. R. Civ. P. 25(d)(1).

[3] Previous pleadings refer to José O. Fabre-Laboy, who was the Secretary at the time when they were filed.

former dairy farmers, as is the Secretary of Agriculture. Not only does the leadership of ORIL, FFIL, and Indulac overlap, but the three entities also operate out of the same facility.

Also joined as a defendant was the Puerto Rico Dairy Farmers Association ("PRDFA"), which represents 300 dairy farmers, who are the producers of the raw milk processed by Tres Monjitas, Suiza, and Indulac.

**2. Background of This Litigation**

This litigation arises out of a history of feuding between dairy farmers and milk processors in Puerto Rico. Milk production in the Commonwealth is seasonal and heavily dependent upon the changing temperature, leading to instability in the seasonal yield of milk and, consequently, waste during months of higher production. The strained relations between farmers and processors and the difficulty of maintaining a consistent supply led to a chaotic situation in an industry essential to the local economy and well-being of the population. To ease tensions between the farmers and processors and to stabilize the disparity between months of lean and fat milk production, Act 34, which was passed June 11, 1957, created ORIL as a regulatory agency to oversee the milk industry. 5 P.R. Laws Ann. § 1093 (2005 & Supp. 2008). From its creation, ORIL set both a maximum price for the sale of milk to consumers and a minimum price for the purchase of raw milk from dairy farmers by milk processors. *See* 5 P.R. Laws Ann. §§ 1096(a), 1107(d) (2005 & Supp. 2008). This means that ORIL regulated both the cost at which milk processors Tres Monjitas and Suiza obtained their raw milk and the price at which they could sell the milk once they processed it into fresh milk. The result of this regulatory structure was such that the price of fresh milk was kept low to make it affordable for

consumers. The price of the raw milk, however, was kept high, based on ORIL's determinations regarding the farmers' costs of production and their reasonable expectations of profits.

While processors were required to purchase all of the dairy farmers' milk, Indulac purchased from the processors any raw milk left over after the market demand for fresh milk was met (referred to as "surplus milk"), in order to avoid waste. Under ORIL's pricing system, Indulac purchased this surplus raw milk from the processors at a price significantly below the price that the processors paid the dairy farmers for their non-surplus raw milk.[4] At first, Indulac processed the surplus raw milk that it purchased from the processors to make butter, cream, cheese, and other dairy products that did not directly compete with the fresh milk produced by plaintiffs.

Trouble began around 1985, however, when Indulac began to produce UHT milk, a non-refrigerated milk substitute, which competes directly with plaintiffs' fresh milk. Essentially, by mandating that plaintiffs pay a high price for raw milk and then requiring them to sell the surplus of that same milk to Indulac at a substantially lower price, ORIL created a scheme in which Tres Monjitas and Suiza were forced to subsidize Indulac, their competitor. The district court found that, but for this ORIL-imposed subsidy from the processors, Indulac would not be able to compete with UHT milk imported

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[4] At first, Indulac paid 10 cents per quart of surplus raw milk, though it would, when it saw fit, contribute more directly to farmers. *Vaquería Tres Monjitas*, No. 04-1840, at *19. In February 2006, ORIL changed this price to 32 cents. *Id.* at *27. The same order set the price milk processors paid for the raw milk at 66 cents per quart. *Id.* at *30.

into Puerto Rico from the continental United States. Thus, Indulac became dependent on this scheme. And, as the only processor authorized to produce UHT milk in Puerto Rico,[5] Indulac amassed 70% of the UHT milk market, with the other portion coming from out-of-state sources.

Moreover, unlike the other milk processors, the price at which Indulac may sell its milk to consumers is not regulated. This lack of regulation as to Indulac's retail price for milk, coupled with the relatively low price at which it could purchase surplus raw milk from plaintiffs, allowed Indulac's profit margin to soar, while the processors struggled. And, since Indulac was able to purchase its raw milk at a deflated price, UHT milk became significantly less expensive than fresh milk — a phenomenon unique to Puerto Rico — causing Indulac's UHT milk to begin to dominate the Puerto Rican milk market.

Aside from enjoying a near-monopoly on UHT milk, Indulac also has broad influence over ORIL's regulatory decisions. When, in 2002, Indulac began to guarantee supplemental minimum payments to farmers for raw milk, it was the Board of Indulac, and not ORIL, which determined what were the dairy farmers' costs and what constituted reasonable profits.[6] And, since the Board of

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[5] Plaintiff Suiza applied for, and was denied, a license to process UHT milk itself.

[6] Indulac's payments to farmers became necessary to remedy the decrease in the farmers' compensation that resulted from the decline of the fresh milk market. The district court explains:

> When the demand for fresh milk falls, less fresh milk is retained and less milk at the higher price went originally into the weighted average calculation . . . from which the farmer is paid for its raw milk. Stated differently, a decrease in the demand

Indulac consisted entirely of dairy farmers,[7] they were essentially setting their own cost of production and margin. Even as late as February 2006, during the course of this litigation, when ORIL raised the price to be paid by Indulac for surplus raw milk to 32 cents per quart from 10 cents per quart, it did so using figures provided by Indulac itself. ORIL held no hearings of any kind, nor did the Administrator conduct any examination into Indulac's operations.

In addition to being forced to subsidize Indulac, Tres Monjitas and Suiza found their financial situation changing from year to year with no forewarning. The district court extensively cataloged these regulatory shifts, of which we highlight but a few. Act 34 requires ORIL to reassess its price structure on a yearly basis and to make necessary adjustments based on the cost of milk production and market demand for milk products. *See* 5 P.R. Laws Ann. §§ 1107(e) (2005 & Supp. 2008). Yet, ORIL employed no set standards to judge the profit margins of milk processors, nor did it publish its rules of cost analy-

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> of fresh milk (made from retained milk) and an increase in the demand for UHT (made from surplus) affected negatively the farmer's average and now the possibility of paying the farmer at the established level.

*Vaquería Tres Monjitas*, No. 04-1840, at *23.

[7] While, initially, the Board of Indulac consisted of a mixture of dairy farmers and milk processors, the farmers increasingly dominated the Board until December of 2002, when its bylaws were officially amended to exclude milk processors altogether. During this time, ORIL's regulations were also amended to dilute the power of milk processors on its Administrative Board. *Vaquería Tres Monjitas*, No. 04-1840, at *24-25; Act of Dec. 19, 2002, No. 278, 5 P.R. Laws Ann. 1099(e) (2005 & Supp. 2008).

sis. ORIL failed, for instance, to adopt a consistent and scientific measurement of shrinkage, which represents the volume of milk regularly lost in the processing stage and is required for an accurate measurement of total production. Additionally, in calculating plaintiffs' profits, ORIL neglected to follow a consistent standard in determining whether to allow income reductions for returns of product, a common variable. The same was true for discounts to agents and promotions, and for the costs and fees of professional experts utilized by plaintiffs to enable compliance with regulations.[8] And, in April of 2007, ORIL, for the first time in its history, began to take plaintiffs' profits from non-milk products into account in its income assessment.[9]

To make matters worse, some of ORIL's estimates have been based on clearly outdated economic figures. For instance, the raw milk rate for fresh milk processors effective in May 2005 used cost numbers from 2003. These calculations failed to account for the tremendous increase in prices of essential production elements such as fuel, electricity, and resin that took place in 2004. Likewise, for its 2005 price order, ORIL used the milk production numbers from 2003, even though 2004's figures demonstrated a significant decline, evidencing a consistent trend of reduced production, which ORIL inexplicably failed to take into account.

Such determinations as to plaintiffs' production costs, the price of raw milk, and the price at which they could sell fresh milk to consumers, allowed ORIL to control the milk processors' rates of return. ORIL chose that

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[8] Such reductions were routinely permitted for Indulac.

[9] In contrast to ORIL's consideration of plaintiffs' non-milk profits, Indulac's non-milk profits were not taken into consideration.

this rate should be 10%,[10] taking that figure from a 1997 average rate of return for milk processors in the United States. Not only was this figure outdated, but it also failed to account for the economic particularities of the Puerto Rican milk industry. In fact, the district court found that ORIL never conducted any reasonable economic study on this matter.

The district court further found that, while defendants' goals were to maintain stable milk production and pricing, their regulatory and market practices had the effect of creating a dire and unsustainable situation in Puerto Rico's milk industry. The low price of Indulac's UHT milk allowed it to dominate the market, even though FFIL acknowledges that fresh milk consumption is preferable for health reasons. And, though the demand for fresh milk was dwindling, Tres Monjitas and Suiza were required to purchase all raw milk produced by dairy farmers at an inflated price, and to sell the ever-increasing surplus to Indulac at a deflated price. Plaintiffs claim that continued regulation in this manner would render them insolvent, leading to the collapse of Puerto Rico's milk industry, as they are the only two entities currently collecting raw milk from the dairy farmers, and are the only entities processing fresh milk for consumers.

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[10] This is merely ORIL's estimated figure. In fact, evidence before the district court showed that plaintiffs never achieved a 10% rate of return, and even suffered heavy losses. In the fiscal year 2001, Tres Monjitas and Suiza jointly sustained loses of six million eight hundred and ninety six thousand dollars ($6,896,000.00). In 2002, their losses totaled eight million three hundred and sixty four thousand dollars ($8,364,000.00); and in 2003, they lost ten million dollars ($10,000,000.00). *See* Motion Requesting Injunctive Relief Under Fed. R. Civ. P. 65(a), Docket No. 2, p. 12.

**B. Procedural History**

On August 13, 2004, Tres Monjitas and Suiza filed a complaint in the United States District Court for the District of Puerto Rico. They sought a declaration under the Federal Declaratory Judgment Act, 28 U.S.C. §§ 2201, *et seq.*, that the decisions, acts and orders issued by the Administrator are unconstitutional. They also sought to enjoin ORIL's regulatory scheme pursuant to Fed. R. Civ. P. 65(a).

Specifically, plaintiffs alleged that ORIL's regulatory structure, which precluded them from making a reasonable profit in their milk business, constituted a confiscation of property in violation of the Takings Clause. *See* U.S. Const. amend. V ("No person shall be . . . deprived of . . . property, without due process of law; nor shall private property be taken for public use, without just compensation."). In addition, they claimed that defendants violated their Fourteenth Amendment due process and equal protection rights by acting in an arbitrary and discriminatory fashion in guaranteeing Indulac a subsidized price to produce UHT milk, and favoring Indulac's interests over those of other milk processors. Plaintiffs' final constitutional claim alleged that defendants' regulatory practices violated the dormant Commerce Clause by unduly restraining interstate commerce in milk. U.S. Const. art. 1, § 8, cl. 3. In addition to their constitutional claims, plaintiffs alleged that defendants violated Puerto Rico state law, because their actions contravened the legislative intent of Act 34.

Pursuant to these claims, on August 20, 2004, plaintiffs moved for a preliminary injunction to preclude the Administrator of ORIL from continuing to implement the complained-of regulatory practices and orders. Plaintiffs claimed that irreparable injury would result if

this scheme were kept in place much longer, as they would soon face insolvency. Their insolvency, plaintiffs argued, would have drastic consequences for the people of Puerto Rico, as Tres Monjitas and Suiza alone have the capacity to process the quantity of fresh milk required to supply the Commonwealth. They contrasted their dire outlooks with evidence of Indulac's high profitability, arguing that preliminary injunctive relief would not harm defendants as much as its absence would harm plaintiffs.

After conducting 51 intensive evidentiary hearings over the course of one-and-a-half years, on July 13, 2007, the district court granted the preliminary injunction, ordering that (1) all milk processors pay the same amount for raw milk, (2) that the Administrator of ORIL develop and implement rational, non-discriminatory parameters for price regulation, and (3) that the Administrator adopt a temporary mechanism to allow plaintiffs to recover a fair rate of return from the year 2003[11] until the implementation of the new regulatory regime (this mechanism is referred to as "regulatory accrual").

Defendants timely appealed, arguing that (a) the district court should have abstained from hearing the case pursuant to the *Burford* abstention doctrine; (b) the portion of the district court's injunction order requiring ORIL, a state entity, to establish a regulatory accrual account constituted issuance of retroactive compensatory relief, in violation of defendant's sovereign immunity; (c) the district court erred in denying defendants' equitable defenses, namely the clean hands doctrine, laches, and

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[11] The district court found that plaintiffs "have suffered for the periods from 2003 to 2007 a Due Process and Equal Protection violation reaching levels of a 'taking.'"

estoppel; and (d) the district court erred in applying the standard for issuance of a preliminary injunction.[12]

## II. Discussion

### A. Abstention

Defendants argue that the district court should have abstained from hearing this case under the doctrine set forth in *Burford* v. *Sun Oil Co.*, 319 U.S. 315 (1943). The district court declined to do so, stating that *Burford* does not apply "when the effect of an entire regulatory scheme is challenged as unconstitutional." *Vaquería Tres Monjitas*, No. 04-1840, at *56 (quoting *Tenoco Oil Co.* v. *Dep't. of Consumer Affairs*, 876 F.2d 1013, 1029 n. 23 (1st Cir. 1989)). We agree.

#### 1. Applicable Law

In *Burford*, the Supreme Court upheld a federal court's decision to abstain from reviewing an order of the Texas Railroad Commission granting Burford a permit to drill oil wells in east Texas. Plaintiff, Sun Oil, had brought suit not to determine the constitutional validity of the state regulation, which had been settled in prior litigation, but to challenge whether the order was reasonable under a state statute. *Burford*, 319 U.S. at 328, 332. While the plaintiffs in *Burford* did allege that the commission order violated their right to due process, resolving the issues on appeal required interpreting state, not constitutional, law. *Id.* at 331. Since the constitutional validity of the commission's complex procedures was not at issue, the Supreme Court recognized that the federal court was simply being called upon to review the state agency's determination in light of the policy out-

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[12] Defendants Indulac and PRDFA also filed motions to stay the injunction pending appeal, which were dismissed voluntarily.

lined by state law. *Id.* at 320-21, 331. On these facts, the Court held that, despite the existence of federal subject matter jurisdiction, abstention was proper to maintain the balance between state control over its own regulatory policies and federal oversight. *Id.* at 327, 332.

Later, in *New Orleans Pub. Serv., Inc.* v. *Council of New Orleans* (*NOPSI*), the Supreme Court clarified that a federal court should abstain from hearing a case that involved "difficult questions of state law bearing on policy problems of substantial public import," or where federal intrusion may prove "disruptive of state efforts to establish a coherent policy with respect to a matter of substantial public concern."[13] 491 U.S. 350, 361 (1989) (citation omitted). We have observed that *NOPSI's* "reformulation" of *Burford*, "can be read expansively or narrowly and is ultimately ambiguous." *Pub. Serv. Co. of New Hampshire* v. *Patch*, 167 F.3d 15, 27 (1st Cir. 1998).

We believe that an expansive reading of *NOPSI* — one that would require federal courts to abstain from hearing any case involving important state regulatory policies-is not consistent with Supreme Court precedent or with our own. Indeed, it would fly in the face of the Supreme Court's repeated admonitions that *Burford* abstention be "the exception, not the rule." *Moses H. Cone Mem'l Hosp.* v. *Mercury Const. Corp.*, 460 U.S. 1, 14 (1983) (internal quotations and citation omitted). Moreover, cases since *NOPSI* have not treated *Burford* as severely curtailing federal courts' jurisdiction. *See, e.g.*, *Quackenbush v. Allstate Ins. Co.*, 517 U.S. 706, 728,

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[13] In *NOPSI*, the Court held that a federal court did not need to abstain from deciding whether the Federal Energy Regulatory Commission's decision that a utility's participation in a nuclear power plant venture was reasonable preempts a state agency's determination of reasonableness of the same issue.

(1996) (stating that "*Burford* represents an extraordinary and narrow exception to the duty of the District Court to adjudicate a controversy properly before it.") (internal quotations omitted). While *Burford* recognizes that states should be given leeway to pursue their prerogatives through their own agencies and courts without federal interference, binding precedent makes clear that a federal court need not abstain from hearing a case involving state regulatory administration "merely because resolution of a federal question may result in the overturning of a state policy." *Zablocki* v. *Redhail*, 434 U.S. 374, 379 n. 5 (1978).

A narrow reading of *NOPSI*, on the other hand, best comports with not only Supreme Court, but also this Circuit's precedent. In *Bath Mem'l Hosp.* v. *Maine Health Care Fin. Comm'n*, we recognized that *Burford* abstention must only apply in "unusual circumstances," when federal review risks having the district court become the "regulatory decision-making center." 853 F.2d 1007, 1012-13 (1st Cir. 1988). Thus, when a federal court's interference would effectively create a dual review structure for adjudicating a state's specific regulatory actions, abstention under *Burford* may be appropriate. *Id.* We observed in Patch that "[t]he fundamental concern in *Burford* [was] to prevent federal courts from bypassing a state administrative scheme and resolving issues of state law and policy that are committed in the first instance to expert administrative resolution." 167 F.3d at 24 (citing *NOPSI*, 491 U.S. at 361-64; *Bath*, 853 F.2d at 1014-15). Abstention is not warranted, however, when a claim requires the federal court to decide "predominating federal issues that do not require resolution of doubtful questions of local law and policy." *Id.*

With this background in mind, we review the district court's decision not to abstain from hearing plaintiffs' claims. The district court's findings of law regarding the requirements of abstention doctrine in the abstract are reviewed *de novo*, while the application of particular facts to that law is reviewed for abuse of discretion. *Sevigny* v. *Employers Ins. of Wausau*, 411 F.3d 24, 26-27 (1st Cir. 2005).

**2. Analysis**

We believe that the district court properly declined to abstain from hearing plaintiffs' claims, as (1) the district court's participation does not disrupt ORIL's role as the regulatory decision-maker or interfere with the agency's ability to apply its expertise to local facts in establishing a coherent state policy; and (2) the heart of plaintiffs' action lies in the constitutional challenge to ORIL's decision-making process as a whole, and not to the reasonableness of their particular determinations.

Defendants argue that plaintiffs' claims require the district court to conduct an inquiry into the specifics of ORIL's orders, pursuant to its own construction of state law and policy, which is precisely the type of intrusion abstention doctrine seeks to avoid. We disagree.

While Tres Monjitas and Suiza certainly allege that ORIL's orders were erroneous in substance, the district court was not required — and specifically declined — to rule on their merits, opting instead to focus on ORIL's decision-making *process*, which it found to be arbitrary on the whole. *Vaquería Tres Monjitas*, No. 04-1840, at *62-67. In discussing the rates of return set by ORIL, for example, the district court expressed the narrowness of its finding:

> The court does not question the established fee per se; the error is in not performing a reasonable, timely economic study setting the reasonable rate and the continuing usage of stale data as to rate of return (1997), and further not considering currently doing business in the Puerto Rican market under current economic realities. *The court does not hint at any figure as to reasonable rate of return.* This rate belongs to the setting by the Administrator, not the court.

*Id.* at *37 (emphasis added). We do not believe that the decisions in the *Burford* line of cases prevent federal courts from undertaking such inquiries.

Furthermore, we refuse to treat, as defendants assert, the district court's review of the facts surrounding the dispute as evidencing the need for abstention. In *Bath*, we voiced our concern about having federal courts "conduct highly individualized review of particular, firm-specific regulatory decisions." 853 F.2d at 1014 (interpreting the Supreme Court's reasoning in *Burford*). Yet, the fact that the district court peered into the substance of ORIL's determinations does not run afoul of our warning in *Bath*. The district court did not examine ORIL's decisions to gauge the wisdom of their outcomes, but rather to determine whether or not they were arbitrary and discriminatory, pursuant to the constitutional questions posed by plaintiffs.

Defendants next argue that, to survive *Burford* abstention, plaintiffs' suit should have taken the form of a facial challenge to Act 34, and not an attack upon ORIL's orders, which it had full authority to promulgate. We be-

lieve this argument is based upon a misconstruction of *Burford*, the subsequent case law, and the case at hand.

In *Burford*, plaintiffs' challenge centered on the reasonableness of a particular administrative order. Since they did not attack either the authority of the Texas Railroad Commission or its adjudicative methods, the constitutional issue was merely a gloss upon the challenge to the administrative decision, the wisdom of which was truly at the heart of the matter. *See Burford*, 319 U.S. at 328 n. 24; *see also Ala. Pub. Serv. Comm'n* v. *S. Ry. Co.*, 341 U.S. 341, 343 (1951) (holding that abstention was proper when the plaintiff's claim consisted of a challenge to an administrative decision born out of a scheme already held constitutional by the Supreme Court).

That is plainly not the case here. Plaintiffs do not claim that ORIL violated their rights to due process, for instance, by issuing an order contrary to state policy. Rather, they claim that the entire system by which ORIL renders its decisions is unconstitutional. As we stated in *Bath*, "abstention in the *Burford* line of cases rest[s] upon the threat to the proper administration of a *constitutional* state regulatory system." 853 F.2d at 1013. In *Tenoco Oil*, we stated even more plainly: "*Burford* abstention does not apply . . . when the effect of an entire state regulatory scheme is challenged as unconstitutional." 876 F.2d at 1028 n.23.

Defendants further contend that, since *Bath* dealt with facial challenges to a state law, and given that *Bath* forms the basis for the above statement in *Tenoco Oil*, neither case applies to the case at hand. This is so, they argue, because plaintiffs do not challenge Act 34 on its face, but rather as it is applied. We believe such a construction to be unduly restrictive.

A federal court need not abstain from hearing a constitutional claim against an administrative scheme simply because the constitutionality of its originating statute is not contested. In *Planned Parenthood League of Massachusetts* v. *Bellotti* (*Bellotti II*), for instance, we held that it was irrelevant for the *Burford* abstention analysis that plaintiffs mounted an "as-applied" challenge to a statute, as opposed to a facial one. 868 F.2d 459 (1st Cir. 1989). *Bellotti II* dealt with a challenge to a Massachusetts statute requiring a minor seeking an abortion to obtain either parental consent or have the restriction waived by a court order. Plaintiffs initially sued to enjoin state officials from enforcing the statute, based on a facial challenge to the law under Articles I, II, X, and XVI of the Massachusetts Declaration of Rights. Injunctive relief was denied, and plaintiffs amended their complaint to include an as applied challenge. *Id.* at 461. The district court dismissed the action, however, out of concern that comity required a federal court to abstain from meddling in the state's internal operations. *Id.* at 462-63; *Planned Parenthood League of Mass.* v. *Bellotti* (*Bellotti I*), 608 F. Supp. 800, 803-05 (D. Mass. 1985). We reversed, holding that abstention was not appropriate, as "what will occur is not an ongoing intermeddling with the state judiciary but a prohibition of an unconstitutional *process.*" *Bellotti II*, 868 F.2d at 465 (emphasis added). We stated that, rather than focusing on either party's characterization of the case, a federal judge must perform an independent evaluation and "assess the *essential nature* of the litigation to see whether its proper objectives could be attained without the intrusion into internal operations of the state judiciary." *Id.* at 466 (emphasis added). We then held that the case was not a proper one for abstention, as plaintiffs' main objective was to enjoin an unconstitutional state process. *Id.* at 465-66.

Like *Bellotti II*, the case at hand involves a challenge to a regulatory process, which places it squarely within the line of cases disfavoring abstention, and it is no impediment that plaintiffs do not mount a facial challenge to Act 34. While federal courts should refrain from entering into the technicalities of states' regulatory apparatuses, they should not decline to hear cases that challenge the whole of those regulatory schemes under the United States Constitution. Plaintiffs do not seek federal review of a price order, nor are they asking the Court to interpret local law. Rather, they seek to have ORIL's current decision-making process invalidated as contrary to the guarantees of due process and equal protection. Theirs is a broad challenge to a regulatory scheme, which plaintiffs contend has no set standards and affords the Administrator unbridled discretion over rate-making. In other words, Tres Monjitas and Suiza do not seek to overturn an administrative decision, but to fundamentally alter the way in which ORIL issues its orders. *See, e.g., id.*, 868 F.2d at 466 ("What PPLM seeks here is not for the federal court to tinker with Massachusetts' scheme of regulating minors' abortions, but for the court to dismantle it."). Abstention is not proper in such circumstances.

Finally, the nature of the injunctive order issued demonstrates that the question presented to the district court was not one as to which the court was required to abstain. The order does not second-guess the Administrator's determinations, nor does it set a new regulatory standard. While the order does set the price to be paid by all processors for raw milk at 55 cents per quart, this figure was not the product of the court's own calculation. Rather, it represents the cost plus fair return rate of the dairy farmers that was last established by ORIL in 2006. In adopting the 55 cent figure, the district court's order

establishes parity among the processors at the level that ORIL itself calculated. Thus, in deferring to ORIL's own findings, the district court does not engage in the sort of fact-specific technical inquiry *Burford* prohibits. Overall, the order requires that ORIL develop and implement reasonable, intelligible standards for future determinations.[14] ORIL remains free to continue to apply its expertise to distinctively local regulatory facts.[15] But, it must do so in a way that protects the Due Process and Equal Protection rights of those subject to its regulations.[16]

Thus, we hold that the district court properly declined defendants' invitation to abstain from entertaining this action.

**B. Eleventh Amendment**

As part of the preliminary injunction granted by the district court, ORIL was ordered to develop and implement a mechanism to compensate Plaintiffs for the deficient rate of return that was mandated by ORIL from the year 2003 until the date of the district court's decision:

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[14] "In a period of no more than thirty (30) days, the Administrator will put into effect nondiscriminatory, rational and scientific regulatory standards that will allow him to determine costs and fair profits return for all the participants in the Puerto Rico regulated milk market." *Vaquería Tres Monjitas*, No. 04-1840, at *94.

[15] "The Administrator shall perform a study as to the economic realities of doing business in Puerto Rico and the particular 'fit' of Puerto Rico into any economic model which may be used from other jurisdictions." *Vaquería Tres Monjitas*, No. 04-1840, at *94.

[16] "When the Administrator eventually determines to change the price to be paid to said dairy farmers, all market participants using raw milk to process fluid milk will pay the same amount for the milk." *Vaquería Tres Monjitas*, No. 04-1840, at *94.

> The Administrator is ordered to adopt a temporary mechanism that will allow the processors to recover the new rate of return they are entitled to (whatever that may be) for the year 2003 (base cost year of the present structure) and up to the day when they begin to recover said rate based on the new regulatory standards and corresponding order. The Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of his choosing.

*Vaquería Tres Monjitas,* No. 04-1840, at 95-96. The mechanism developed by the parties involved a small surcharge[17] to be applied to every quart of milk sold in the Commonwealth, which would then be placed into an accrual account for the benefit of Tres Monjitas and Suiza.

On appeal, defendants contend that this order calls for retroactive compensatory relief, which is barred by the Eleventh Amendment. Plaintiffs respond that such relief is allowed, even if the regulatory accrual were to be characterized as retroactive, as it would be derived from milk consumers only, and not from the coffers of the Commonwealth. We agree that the Eleventh Amendment is not implicated.

**1. Applicable Law**

The Eleventh Amendment states that "[t]he Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign

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[17] As it stands, the surcharge is 1.5 cents per quart.

State." U.S. Const. amend. XI. The Supreme Court has held that the doctrine of sovereign immunity reaches beyond the words of the Eleventh Amendment, extending immunity to state governments in suits not only by citizens of another state, but by its own citizens as well. *Alden* v. *Maine*, 527 U.S. 706 (1999). An administrative arm of the state is treated as the state itself for the purposes of the Eleventh Amendment, and it thus shares the same immunity. *See Hafer* v. *Melo*, 502 U.S. 21, 25 (1991); *see also Pastrana-Torres* v. *Corporación de P.R.*, 460 F.3d 124, 126 (1st Cir. 2006) ("[Eleventh Amendment] immunity applies only to the states themselves and entities that are determined to be arms of a state.").

While a state may not be sued directly absent its own consent, the *Ex Parte Young* doctrine permits suits to proceed against state officers in their official capacities to compel them to comply with federal law. *Ex Parte Young*, 209 U.S. 123 (1908). This stems from the notion-some say fiction-that, since a state could not authorize an official to violate federal law, by doing so, a state official is stripped of her authority and thus a suit against her does not implicate the state's sovereign immunity. *Id.* at 159-60; *see also Pennhurst State School and Hospital* v. *Halderman*, 465 U.S. 89, 102-03, 105 (1984) (discussing the "fiction of *Young*"). Such suits, however, may only seek prospective injunctive or declaratory relief; they may not seek retroactive monetary damages or equitable restitution. *Edelman* v. *Jordan*, 415 U.S. 651, 664-65 (1974). If the court were to order a state official in her official capacity to dispense compensatory relief, the monies would be drawn from the state treasury and run afoul of the Eleventh Amendment. *Id.* at 664. We have observed that "[t]he line drawn by the Court represents a compromise between the impulse to preserve state autonomy and the need to enforce federal law. Injunctions

are necessary to assure the supremacy of national law; damage awards are not." *Santiago* v. *Corporación De Renovación Urbana Y Vivienda De P.R.*, 554 F.2d 1210, 1212 (1st Cir. 1977).

**2. Analysis**

The issue here is whether or not the manner of relief ordered by the district court runs afoul of the Eleventh Amendment's prohibition against retroactive damages that reach the state treasury. Since the harm to be remedied by the district court's regulatory accrual order was the deficient rate of return imposed upon Tres Monjitas and Suiza since 2003, defendants argue that it is necessarily backward-looking, and thus barred by Supreme Court and First Circuit precedent.

Plaintiffs urge this court to reject these arguments on either of two possible grounds. First, plaintiffs maintain that the regulatory accrual is not meant to compensate Tres Monjitas and Suiza for the revenue lost under ORIL's scheme, but rather to rebuild their capital bases, which are, collectively, $5 million in the red. They claim that, even if the price of milk were raised to allow a reasonable rate of return, the processors could not make any profit until they rebuild their capital bases, meaning that the regulatory accrual is a necessary component of any prospective relief awarded. Plaintiffs alternatively argue that, even if the form of relief is deemed retroactive, sovereign immunity should present no bar, as none of the compensation would come from the state treasury.

We decline to rule on plaintiffs' characterization of the regulatory accrual as prospective, as we believe that their second argument sufficiently supports their position.

Defendants argue that it is irrelevant whether or not the remedy ultimately is derived from the state treasury, citing *Edelman* for the proposition that prospective relief is available even if compliance therewith requires expenditures from the state treasury, but retrospective relief is always prohibited. *Edelman*, 415 U.S. at 667-68. We are not so convinced.

Defendants provide no support for their contention that retrospective relief *that does not reach the state treasury* is barred by sovereign immunity. Rather, the cases cited by defendants, including *Edelman*, involve requests for retroactive compensation that would invariably come out of state treasuries. *See, e.g., id.* at 667 ("[Relief sought] requires payment of state funds, not as a necessary consequence of compliance in the future with a substantive federal-question determination, but as a form of compensation. . . . "); *Papasan* v. *Allain*, 478 U.S. 265, 279 (1986) (plaintiffs sought funds directly from the state to fund school districts).

In fact, both the Supreme Court and this Circuit have consistently considered the source of relief as being of paramount importance to Eleventh Amendment considerations. In *Hess* v. *Port Authority Trans-Hudson Corp.*, the Supreme Court noted that "the impetus for the Eleventh Amendment [is] the prevention of federal-court judgments that must be paid out of a State's treasury." 513 U.S. 30, 48 (1994). In even stronger terms, the Court later added, "[i]n sum . . . the vast majority of Circuits . . . have concluded that the state treasury factor *is the most important factor to be considered . . . and, in practice, have generally accorded this factor dispositive weight.*" *Id.* at 49 (emphasis added) (internal quotations and citations omitted). This Circuit has followed this mandate. In *Libby* v. *Marshall*, we stated:

> The damage the Eleventh Amendment seeks to forestall is that of the state's fisc being subjected to a judgment for compensatory relief. Only if the state is forced to use funds from the state treasury to satisfy a compensatory judgment do the adverse consequences that the Eleventh Amendment prohibits occur.

833 F.2d 402, 406 (1st Cir. 1987).

Here, the money in question would come directly from consumers of milk in Puerto Rico. Unlike a tax, it would be neither collected by government entities nor retained in the Commonwealth's treasury. Apart from the initial price order, no state action is required to implement this remedial scheme, which would, in no way, reach the coffers of the Commonwealth. Thus, because no state funds are implicated by the district court's order, we hold that the Eleventh Amendment's prohibition against retrospective relief does not apply.

Defendants alternatively argue that the regulatory accrual is impermissible by attempting to frame the relief as, in essence, ordering the payment of monetary damages in just compensation for a regulatory taking. They then argue that several circuits have dismissed Takings Clause actions against state officials in their official capacities, as the Eleventh Amendment bars a federal court from issuing just compensation relief against a state entity. For this proposition, they cite *Seven Up Pete Venture* v. *Brian Schweitzer,* 523 F.3d 948 (9th Cir. 2008), and *DLX* v. *Kentucky,* 381 F.3d 511 (6th Cir. 2004). Defendants also point to this Circuit's precedent, including *Ortiz De Arroyo* v. *Romero Barceló,* 765 F.2d 275, 280 (1st Cir. 1985), which states that,

in a case involving governmental deprivation of property in violation of the Fifth and Fourteenth Amendments, "the court may not award the value of the diminished property right; it may issue only declaratory or injunctive relief." *See also Culebra Enter. Corp.* v. *Rivera Ríos*, 813 F.2d 506, 512 (1st Cir. 1987); *Citadel Corp.* v. *P.R. Highway Auth.*, 695 F.2d 31, 33 (1st Cir. 1982); *Pamel Corp.* v. *P.R. Highway Auth.*, 621 F.2d 33, 36 (1st Cir. 1980).

We are not persuaded, however, that the present situation should be analyzed under defendants' characterization. Unlike any of the cases relied upon by defendants, here there has been no award of damages that the state must pay. That an equitable remedy results in the payment of monies to plaintiff does not, in itself, render the relief monetary compensation for a taking. The district court's order does not require ORIL or the Department of Agriculture to provide just compensation, or any monetary award for that matter. As we have stated above, no measure of relief fashioned by the district court would come from the state treasury. Defendants have argued that this scheme is no different from a federal court ordering the levying of a tax to pay equitable restitution, which they contend no federal court has done. Yet, whether Puerto Rico could levy a special tax to compensate Tres Monjitas and Suiza is not the issue before this Court. Unlike a tax, the milk surcharge of 1.5 cents per quart does not rely on the state as an intermediary. Instead, the regulatory accrual operates as any other regulation that raises by a small fraction the price of milk for consumers, based on ORIL's determinations regarding milk processors' costs, revenues, and rates of return.

For the foregoing reasons, we hold that the Eleventh Amendment does not bar the form of relief granted by the district court in its preliminary injunction.

### C. Equitable Defenses

Defendants contend that the district court erred in rejecting their equitable defenses of unclean hands, laches, and estoppel. We review the lower court's ruling for abuse of discretion. *School Union No. 37* v. *Ms. C.*, 518 F.3d 31, 35 (1st Cir. 2008); *Ansin* v. *River Oaks Furniture, Inc.*, 105 F.3d 745, 757 (1st Cir. 1997).

#### 1. Unclean Hands

Our courts have long held the view that "[h]e who comes into equity must come with clean hands." *Dr. José S. Belaval, Inc.* v. *Pérez-Perdomo*, 488 F.3d 11, 15 (1st Cir. 2007) (quoting *Keystone Driller Co.* v. *Gen. Excavator Co.*, 290 U.S. 240, 241 (1933)). This is to say that we are skeptical of those who seek equitable relief when they themselves have engaged in misconduct. For the defense to apply, we have also routinely stated that the misconduct must be "directly related to the merits of the controversy between the parties." *Id.* (internal quotations omitted).

Defendants seek to invoke this defense, arguing that "plaintiffs directly participated and approved the decision to aggressively market Indulac's UHT milk and benefitted from the results thereof." Whether or not this were true, this allegation does not implicate the unclean hands defense, as defendants fail to show-or even explain-how such actions constitute "misconduct" on the part of the plaintiffs.

As the district court could have reasonably concluded from the facts that plaintiffs were not complicit in any

wrongdoing related to the merits of this controversy, we hold that it did not abuse its discretion in rejecting defendants' unclean hands defense.

**2. Laches**

The doctrine of laches may bar a claim that was raised after an inexcusable delay. "In order for laches to apply, the district court must examine whether plaintiff's delay in bringing suit was unreasonable and whether defendant was prejudiced by the delay." *Puerto Rican-American Ins. Co.* v. *Benjamin Shipping Co. Ltd.*, 829 F.2d 281, 283 (1st Cir. 1987) (citing *Costello* v. *United States*, 365 U.S. 265, 282 (1961)).

According to defendants, Tres Monjitas and Suiza began experiencing losses as early as 1998, but waited until 2004 to bring any claims. Such "slumber," they argue, voided their claims for equitable relief.

Defendants, however, have not presented any evidence indicating that the delay was either unreasonable or prejudicial, nor have they made more than a half-hearted attempt to do so. As a result, their argument fails. First, as the district court found, "before the filing of this complaint, plaintiffs and the Administrator were still meeting to try to reach a solution . . . ." *Vaquería Tres Monjitas*, No. 04-1840, at *11. It would be unwise and inequitable to punish Tres Monjitas and Suiza for attempting to settle their grievances through administrative remedies and negotiations. Second, nowhere in their brief to this court do defendants even allude to the issue of prejudice. They do not allege that they have been in any way injured by the lapse of time, nor have they shown that the passage of time has eroded "the memory and life of witnesses, the muniments of evidence, and other means of proof." *Costello*, 365 U.S. at

282 (quoting *Brown* v. *Buena Vista County*, 95 U.S. 157, 161 (1877)) (internal quotation marks omitted).

Considering that defendants have failed to satisfy the standard for the application of the laches doctrine, we hold that the district court did not abuse its discretion in failing to dismiss the action on that basis.

**3. Estoppel**

Under 28 U.S.C. § 1738, federal courts must give "full faith and credit" to the judgments arising out of state courts and give them the same preclusive effect as would a court of that state. Thus, a decision in state court collaterally estops relitigation in a later action in federal court. *Allen* v. *McCurry*, 449 U.S. 90, 104-05 (1980) (preventing relitigation of habeas corpus claim already decided in state court).

Defendants contend that, under Puerto Rican law, "an administrative decision not reviewed by the party adversely affected becomes final and firm as a commonwealth judgment." *Acevedo* v. *Western Digital Caribe, Inc.*, 140 P.R. Dec. 452, 465-66 (P.R. 1996) (internal citation omitted). They then argue that, as the facts found in the orders issued by ORIL from 1998 to 2002 were never challenged, they are "final and firm" and hold the same preclusive effect as the decisions of a court of Puerto Rico, rendering them unassailable in subsequent court actions. *Pastor-Ginorio* v. *R & G Mortg. Corp., Inc.*, 371 F. Supp. 2d 89, 92 (D.P.R. 2005).

This argument strains credibility. Under Puerto Rican law, a claim may be precluded under the doctrine of res judicata if there exists "the most perfect identity between the things, causes, and persons of the litigants, and their capacity as such." 31 P.R. Laws Ann. § 3343. Res judicata cannot apply here to bar Tres Monjitas' and

Suiza's claims, as there has not been a prior court decision on these issues, in an action between these same parties in interest. In addition, res judicata will present no obstacle "when the litigant was denied a 'full and fair opportunity to litigate' his claims in the earlier proceeding; in this situation, application of res judicata would violate due process of law." *Arecibo Radio Corp.* v. *Com. of P.R.*, 825 F.2d 589, 592 (1st Cir. 1987) (quoting *Allen*, 449 U.S. at 101).

Tres Monjitas and Suiza frequently received inadequate notice and opportunity to challenge ORIL's regulatory decisions. For example, a 2007 order for the first time took into consideration plaintiff's income from unregulated non-milk products. This new parameter was imposed upon plaintiffs without prior notice or opportunity to be heard. ORIL similarly held no hearings of any sort when it readjusted the percentage of plaintiffs' participation in school lunch programs, decreasing Suiza's share by 5.06% and giving it to Tres Monjitas. Time and time again, ORIL set and reset regulations relating to the measurement of the processors' milk production and income without giving plaintiffs an explanation or a reasonable opportunity to challenge the decisions.

Also, since defendants have clearly stated that they do not wish to challenge the district court's findings of fact, we do not see how their invocation of *Pastor-Ginorio* serves their argument. Even if the Administrator's determinations of facts are to be given preclusive effect, the orders issued did not contain any adjudicatory decisions or rulings of law that are immune from review.

Overall, defendants' argument assumes too much. Their construction of the law would have us hold that the decisions of ORIL's Administrator become unreviewable simply by his say-so. This we cannot do. We hold that the

district court did not abuse its discretion in rejecting defendants estoppel defense.

**D. Preliminary Injunction**

The district court granted the preliminary injunction after finding that the plaintiffs' claims met the traditional four-part test, which requires consideration of (1) the likelihood that the moving party will succeed on the merits; (2) the possibility that, without an injunction, the moving party will suffer irreparable harm; (3) the balance of relevant hardships as between the parties; and (4) the effect of the court's ruling on the public interest. *Waldron* v. *George Weston Bakeries Inc.*, 570 F.3d 5, 9 (1st Cir. 2009).

On appeal, defendants contend that the court erred in its application of the four-part preliminary injunction standard. In addition, they argue that the court's order improperly changed the status quo by transforming Puerto Rico's milk regulatory scheme, whereas the specific purpose of a preliminary injunction is to maintain current conditions until the dispute is decided on the merits.

We review the district court's grant of the preliminary injunction for abuse of discretion. *Waldron*, 570 F.3d at 9. We will set aside the ruling "only if [we are] persuaded that the lower court mistook the law, clearly erred in its factual assessments, or otherwise abused its discretion in granting the interim relief." *McGuire* v. *Reilly*, 260 F.3d 36, 42 (1st Cir. 2001). Within this assessment, findings of fact are reviewed for clear error, and conclusions of law are reviewed *de novo*, while "[j]udgment calls and issues that demand the balancing of conflicting factors are reviewed deferentially." *Wine &*

*Spirits Retailers, Inc.* v. *Rhode Island*, 418 F.3d 36, 46 (1st Cir. 2005) (internal citations omitted).

**1. Likelihood of Success**

After extensively analyzing the factual record and the claims put forth, the district court found that there existed a likelihood that Tres Monjitas and Suiza would succeed on the merits of their claims. In particular, the court found:

> [V]iolations of Due Process, Equal Protection and the Takings Clause, a pattern of lack of standards, change in standards with unfettered discretion, use of stale figures, and lack of an appropriate standard as to fair rate of return in the regulations set by the regulator all pointing to a taking "pursuant" to *Duquesne Light Co. [*v. *Barasch*, 488 U.S. 299, 307 (1989)] and *Tenoco Oil*, 876 F.2d at 1026-1027.

*Vaquería Tres Monjitas*, No. 04-1840, at *91. Defendants challenge this determination as to plaintiffs' Takings Clause, Due Process, and Equal Protection Claims.

However, we need only find that one of the district court's bases for granting injunctive relief is proper to affirm the grant of the preliminary injunction. We believe that sufficient evidence exists in the record to support the district court's determination that Tres Monjitas and Suiza have a likelihood of success on the merits of their Due Process claims.[18]

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[18] Since the Due Process Clause violation is sufficient for the district court's grant of injunctive relief, we see no need to reach the Court's determinations regarding the likelihood of success on the Equal Protection and Takings Clause claims. That we refrain from reach-

Plaintiffs' Due Process challenge arises out of their assertion that the regulatory structure of the Puerto Rican milk industry was beholden to the whims of the Administrator. In addition, they claim that the use of unscientific, stale, and clearly erroneous figures regarding production costs and rates of return nearly drove them out of business. These circumstances, plaintiffs argue, were made possible by the lack of operating standards, which gave the Administrator unchecked power to issue arbitrary determinations. They cite as evidence numerous instances, recounted above, in which the standards ORIL utilized to calculate their income, milk production, or profits changed without warning or rationale.

Defendants argue that allowing Indulac to process surplus milk into UHT and other milk by-products was a reasonable way to support dairy farmers year-round, quell disputes between the farmers and processors, and avoid waste. They cite the difficulty of producing a reliable supply of milk in Puerto Rico as dictating a need for regulation and for the role played by Indulac in stabilizing milk production. Thus, they argue, since these regulations are rationally related to a legitimate government purpose, they meet the requirements of due process, and the district court therefore erred in finding that plaintiffs had a likelihood of success on the merits of their claims.

The Supreme Court has cautioned that courts should refrain from substituting their regulatory wisdom for that of the legislature, explaining that a court's Due Process inquiry should be satisfied "[i]f the laws passed are seen to have a reasonable relation to a proper legisla-

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ing these issues should not be regarded as a commentary on their relative merits.

tive purpose, and are neither arbitrary nor discriminatory." *Nebbia* v. *New York*, 291 U.S. 502, 537 (1934). Likewise, in *Tenoco Oil*, we recognized that this inquiry should focus on "whether a program's procedures are inadequate or whether, overall, a program is arbitrary, discriminatory or irrelevant to a legitimate legislative goal." 876 F.2d at 1021 (citing *Pennell* v. *City of San Jose*, 485 U.S. 1, 11 (1988)). Based on these standards, we have no trouble finding that the district court did not abuse its discretion in finding that plaintiffs had a likelihood of success on their Due Process claims.

First, while the district court agreed with defendants that Puerto Rico has a legitimate state interest in stabilizing milk production and protecting the livelihoods of dairy farmers, it found there was no rational nexus between the regulatory scheme established by ORIL and these goals. *Vaquería Tres Monjitas*, No. 04-1840, at *59-60. The regulations clearly benefit Indulac, a processor of UHT milk, to the detriment of Tres Monjitas and Suiza, the only fresh milk processors in Puerto Rico. As a result of plaintiffs' forced subsidy, Indulac's market dominance depleted the fresh milk market and injured key components of the milk industry, the processors, to the point of near-insolvency. While the Administrator could have rationally decided that Indulac's operation would provide a stabilizing effect, the measures that it took appear to have been specifically engineered to achieve the opposite result — the benefit of Indulac to the detriment of the milk processors and, ultimately, the milk market. Thus, the district court reasonably concluded that the scheme created by ORIL cannot satisfy rational basis review, as "the elimination of one of the components of the industry is 'demonstrably irrelevant to the policy the Legislature is free to adopt.'" *Vaquería*

*Tres Monjitas*, No. 04-1840, at *71 (quoting *Tenoco Oil*, 876 F.2d at 1024).

Second, the district court found that the means used to achieve ORIL's goals did not pass constitutional muster. The record is replete with examples of regulatory practices employed by ORIL that support the district court's finding that the regulatory scheme was arbitrary, and thus violated due process. *See Nebbia*, 291 U.S. at 537. The Administrator repeatedly altered — without notice or explanation — the standards for calculating plaintiffs' incomes and production figures. Essential parameters for the adjustment of gross income based on customer returns and discounts to distributors, for instance, were capriciously applied or ignored. The shrinkage factor, a measurement of the fraction of milk lost in the processing phase, seems to have been set and adjusted at random. In fact, in many instances, the district court found that the Administrator had not performed any inquiries, studies, or anything resembling the diligent research one would expect from a rate-making agency before issuing orders. Accordingly, the court reasonably concluded that the standards and regulations set forth by ORIL, taken as a whole, likely violated plaintiffs' due process.

Ultimately, the district court concluded that the record reasonably supported a finding that defendants failed to meet the standards for rate-making as set out by the Supreme Court and this Circuit. Given the ample evidence of arbitrary and discriminatory regulation, we see no abuse of discretion in the court's determination that plaintiffs have demonstrated a likelihood of success on the claim that defendants' actions constituted a regulatory taking of their property without due process.

### 2. Irreparable Harm

The district court found that a denial of plaintiffs' request for a preliminary injunction could lead to irreparable harm to Tres Monjitas and Suiza. More specifically, it stated that defendants' actions, absent injunctive relief, "point to permanent loss in market and long-standing violations of constitutional rights for extensive protracted periods of time." *Vaquería Tres Monjitas,* No. 04-1840, at *91.

Defendants argue that the alleged harm the district court ruled irreparable was, in fact, economic harm, which can be remedied through money damages, and thus does not warrant injunctive relief. The matter is a close one, but ultimately, we defer to the district court's decision.

While certain constitutional violations are more likely to bring about irreparable harm, we have generally reserved this status for "infringements of free speech, association, privacy or other rights as to which temporary deprivation is viewed of such qualitative importance as to be irremediable by any subsequent relief." *Pub. Serv. Co. of New Hampshire* v. *West Newbury,* 835 F.2d 380, 382 (1st Cir. 1987). So, it cannot be said that violations of plaintiffs' rights to due process and equal protection *automatically* result in irreparable harm.

Also, it has long been held that traditional economic damages can be remedied by compensatory awards, and thus do not rise to the level of being irreparable. *Puerto Rico Hosp. Supply, Inc.* v. *Boston Scientific Corp.,* 426 F.3d 503, 507 (1st Cir. 2005). Yet, it has also been recognized that some economic losses can be deemed irreparable. For instance, "an exception exists where the potential economic loss is so great as to threaten the existence

of the movant's business." *Performance Unlimited, Inc.* v. *Questar Publishers, Inc.*, 52 F.3d 1373, 1382 (6th Cir. 1995) (citing *Doran* v. *Salem Inn, Inc.*, 422 U.S. 922, 932 (1975) (finding no abuse of discretion in determination that "absent preliminary relief [movants] would suffer a substantial loss of business and perhaps even bankruptcy")); *see also Nat'l Screen Serv. Corp.* v. *Poster Exchange, Inc.*, 305 F.2d 647 (5th Cir. 1962) (affirming grant of preliminary injunction where denial of injunctive relief would result in the destruction of movant's business).

In addition, we have held that the irreparable harm requirement may be met upon a showing that "absent a restraining order, [a party] would lose incalculable revenues and sustain harm to its goodwill." *Ross-Simons of Warwick, Inc.* v. *Baccarat, Inc.*, 102 F.3d 12, 19 (1st Cir. 1996). In addition, in *Automatic Radio Mfg. Co.* v. *Ford Motor Co.*, we suggested that the inability to supply a full line of products may irreparably harm a merchant by shifting purchasers to other suppliers. 390 F.2d 113, 116-17 (1st Cir. 1968).

Moreover, the measure of irreparable harm is not a rigid one; it has been referred to as a sliding scale, working in conjunction with a moving party's likelihood of success on the merits. *See Ross-Simons*, 102 F.3d at 19 ("[A]n attempt to show irreparable harm cannot be evaluated in a vacuum; the predicted harm and the likelihood of success on the merits must be juxtaposed and weighed in tandem."); *see also EEOC* v. *Astra USA, Inc.*, 94 F.3d 738, 743 (1st Cir. 1996) ("[W]hen the likelihood of success on the merits is great, a movant can show somewhat less in the way of irreparable harm and still garner preliminary injunctive relief."); *Gately* v. *Massachusetts*,

2 F.3d 1221, 1232 (1st Cir. 1993) ("[I]rreparable harm is subject to a sliding scale analysis . . . .").

Finally, we are mindful of the narrowness of our charge, recognizing that considerable deference is owed to the district court in evaluating this prong of the preliminary injunction standard. "District courts have broad discretion to evaluate the irreparability of alleged harm and to make determinations regarding the propriety of injunctive relief." *K-Mart Corp.* v. *Oriental Plaza, Inc.*, 875 F.2d 907, 915 (1st Cir. 1989) (internal quotations omitted).

With the guidance of precedent, we look to the district court's finding and do not see any abuse of discretion in applying the facts to the legal standard. Clearly, plaintiffs have suffered economic harm. But, that is not the full extent of their injury. As found by the district court, Tres Monjitas and Suiza have continued to subsidize Indulac's production of UHT milk, undercutting their own goodwill by propping up their competitors. As a result, they have suffered a steady decline in the market for fresh milk and are on the verge of losing their businesses. After suffering years of losses, their capital bases have been depleted by five million dollars, and the district court found both companies to be on the brink of insolvency.

Taking into account the rapidly eroding state of the Puerto Rican milk industry, the need for immediate relief, and the likelihood of plaintiffs' success on the merits of their claims, we do not believe the district court abused its discretion in finding that the gravity of these dire circumstances, if allowed to run their course, would constitute irreparable harm, and that their imminence called for preliminary injunctive relief.

### 3. Balance of Equities

The district court found, in considering the balance of equities between plaintiffs and defendants, that "[t]he matter is not close." *Vaquería Tres Monjitas*, No. 04-1840, at *92. In balancing the harm likely caused to the milk processors without the injunction with the harm its grant would cause defendants, the Court stated that "[t]he constitutional rights of plaintiff[s] override, with [their] consequential permanent loss of market and potential fire sale of its plants, the rights of defendant to continue with a preferential purchase price of raw milk which is prima facie discriminatory." *Id.*

On appeal, defendants entreat us to overturn the district court's determination, arguing that the hardships caused by the preliminary injunction outweigh the alleged harm to Tres Monjitas and Suiza absent the order. In particular, they allude to the injury that will come to Indulac, the dairy farmers and their cattle, the stability of the milk supply, and the existing regulatory structure.

In reviewing the district court's judgment of this issue, we must refrain from second-guessing the district court's assessment, unless we find that the court abused its discretion. *See George Weston Bakeries*, 570 F.3d at 8 ("[W]e afford considerable deference to the trial court's balancing of equities."); *see also Wine & Spirits Retailers*, 418 F.3d at 46 ("[J]udgment calls and issues that demand the balancing of conflicting factors are reviewed deferentially.").

We find in the record no reason to second-guess the district court's finding, arrived at in the course of over a year of hearings and testimony, that the balance of equities at play with this injunction favors the plaintiffs. The district court viewed Tres Monjitas' and Suiza's situa-

tions as desperate — both having negative capital bases and facing insolvency. Furthermore, we see no reason why ORIL cannot stabilize milk production and protect dairy farmers, while setting rational regulations based on non-arbitrary and non-discriminatory standards. So, while we are sympathetic to defendants' claims of hardship, this is a situation of their own doing, and further, we do not believe the district court erred in according greater weight to plaintiffs' hardships in the event that injunctive relief were not granted.

**4. Public Interest**

The district court found that the "public interest lies in the granting of the injunctive relief." *Vaquería Tres Monjitas*, No. 04-1840, at *92. It noted that the current situation is unsustainable for the Puerto Rican milk industry as a whole. The dominance of artificially underpriced UHT milk in the market has diminished the market for processors' fresh milk to the point where Indulac's "surplus" has grown beyond its capacity. Ever-decreasing revenues from Tres Monjitas and Suiza mean lower subsidies to Indulac and FFIL, causing depletion of the Fund, which in turn is threatening the dairy farmers' livelihoods. *Id.* at 39-41. In light of these facts, the district court concluded that "[w]ithout the injunctive relief, the plants are close to being sold at very low prices, an important independent element of the industry is about to be lost and the industry is then close to being monopolized by one party of the milk industry." *Id.* at *92.

Again, we must give deference to the district court's assessment of the situation. We find ample support in the factual record for its determination, and hold that it did not abuse its discretion in finding that the granting preliminary injunctive relief was in the public interest.

### 5. Scope of Relief

Lastly, defendants challenge the scope of the relief granted by the district court. They contend that the Court "erred in issuing injunctive relief that forever changed the status quo-contrary to the purposes of the preliminary injunctive relief." We disagree.

We first note that "[i]njunctions must be tailored to the specific harm to be prevented." *Ross-Simons of Warwick, Inc.* v. *Baccarat, Inc.*, 217 F.3d 8, 14 (1st Cir. 2000). Since the district court is in the best position to tailor the scope of injunctive relief to the its factual findings, our review is for abuse of discretion only. *Id.*

The district court found that ORIL had subjected plaintiffs to ongoing constitutional violations as part of an arbitrary and discriminatory regulatory process. In requiring ORIL to develop a scheme that conformed to constitutional principles, the preliminary injunction cut to the heart of the violations. And, by leaving decisions regarding specific pricing figures to the agency, the Court ensured that the preliminary injunction would prove "no more burdensome to the defendant than necessary to provide complete relief." *Tamko Roofing Products, Inc.* v. *Ideal Roofing Co., Ltd.*, 282 F.3d 23, 40 (1st Cir. 2002) (quoting *Califano* v. *Yamasaki*, 442 U.S. 682, 702 (1979)). Indeed, it is difficult to see how the district court overstepped its bounds, when it left the essential parameters of the relief largely in the hands of the defendants.

As to defendants' argument, it cannot be said that the only purpose of a preliminary injunction is to preserve current conditions pending adjudication. That is not to say that defendants' position lacks support. *See CMM Cable Rep., Inc.* v. *Ocean Coast Properties, Inc.*, 48 F.3d

618, 620 (1st Cir. 1995) ( "The court's interim injunctive decree attempts to prevent further injury by maintaining the status quo."). But, taking steps necessary to assure the continued operations of the moving party is appropriate, if the non-moving party's actions threaten its destruction. Thus, in its injunctive order, the district court did not act improperly in requiring ORIL to take steps necessary to ensure the survival of Tres Monjitas and Suiza during the litigation. Contrary to defendant's baffling assertion that the relief "forever changed the status quo," the aim of the order was to establish parity among the milk processors pending outcome of the litigation.

Finally, the potential for a moving party's likelihood of success and showing of irreparable harm can guide the scope of preliminary injunctive relief. Having already found that Tres Monjitas and Suiza had a likelihood of success on the merits of their constitutional claims, the district court was well within its discretion and power to require ORIL to establish non-arbitrary and non-discriminatory regulations to preserve the solvency of the milk processors, which it found to be in imminent jeopardy.

## III. Conclusion

In summation, we hold that the district court did not err in rejecting defendants' *Burford* abstention and Eleventh Amendment immunity arguments, or in rejecting their equitable defenses. We also hold that the district court did not abuse its discretion in granting plaintiffs' motion for a preliminary injunction. The order of the district court is affirmed.

***Affirmed.*** Costs are assessed against appellants.

## APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

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No. 07-2240

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VAQUERÍA TRES MONJITAS, INC.; SUIZA DAIRY, INC., Plaintiffs, Appellees,

*v.*

CYNDIA E. IRIZARRY, in her official capacity as Administrator of the Office of the Milk Industry Regulatory Administration for the Commonwealth of Puerto Rico, Defendant, Appellant,

JOSÉ O. FABRE-LABOY, in his official capacity as Secretary of the Department of Agriculture of the Commonwealth of Puerto Rico; INDUSTRIA LECHERA DE PUERTO RICO, INC. (INDULAC), PUERTO RICO DAIRY FARMERS ASSOCIATION, Defendants.

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No. 07-2369

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VAQUERÍA TRES MONJITAS, INC.; SUIZA DAIRY, INC., Plaintiffs, Appellees,

*v.*

JAIME RIVERA-AQUINO, in his official capacity as Secretary of the Department of Agriculture of the Commonwealth of Puerto Rico; Defendant, Appellant,

INDUSTRIA LECHERA DE PUERTO RICO, INC. (INDULAC); PUERTO RICO DAIRY FARMERS ASSOCIATION; CYNDIA E. IRIZARRY, in her official capacity as Administrator of the Office of the Milk Industry Regulatory Administration for the Commonwealth of Puerto Rico, Defendants.

March 11, 2010

Before LYNCH, Chief Judge, TORRUELLA, BOUDIN, LIPEZ, and HOWARD, Circuit Judges.

## ORDER OF COURT

The petition for rehearing having been denied by the panel of judges who decided the case, and the petition for rehearing en banc having been submitted to the active judges of this court and a majority of the judges not having voted that the case be heard en banc, it is ordered that the petition for rehearing and the petition for rehearing en banc be denied.

TORRUELLA, Circuit Judge, concurring in the denial of en banc review.

Although "the difference between the type of relief barred by the Eleventh Amendment and that permitted under *Ex parte Young* will not in many instances be that between day and night," *Edelman* v. *Jordan*, 415 U.S. 651, 667 (1974), I believe that the panel opinion in this

case is eminently correct in holding that the Eleventh Amendment does not bar the relief afforded by the district court. This ruling is correct because it is consistent with well-established precedent that places decisive weight on the impact a judgment has on the state treasury. *See Hess* v. *Port Auth. Trans-Hudson Corp.*, 513 U.S. 30, 49, 115 (1994) ("[T]he vast majority of Circuits . . . have concluded that the state treasury factor is the most important factor to be considered . . . and, in practice, have generally accorded this factor dispositive weight") (first alteration in the original) (internal quotation marks omitted); *Libby* v. *Marshall*, 833 F.2d 402, 406 (1st Cir. 1987) (stating that "[t]he damage the Eleventh Amendment seeks to forestall is that of the state's fisc being subjected to a judgment for compensatory relief"). In this case the Eleventh Amendment poses no bar to relief because there is simply no impact on the state fisc, *at present or in the future.*

In our November 23, 2009 opinion, we affirmed the district court's grant of a preliminary injunction against the Milk Industry Regulation Administration for the Commonwealth of Puerto Rico ("ORIL" by its Spanish acronym). In its opinion and order, the district court found that Plaintiffs had shown a likelihood of success on the merits of their claim that ORIL put into place an arbitrary and discriminatory regulatory scheme that violated the Due Process, Equal Protection and Takings clauses of the United States Constitution. As part of the preliminary injunction, the district court directed ORIL to adopt a regulatory mechanism to compensate Plaintiffs for the deficient rate of return that was imposed by ORIL's regulatory scheme from the year 2003. In compliance with the district court's injunctive order, ORIL adopted an administrative order which directed that 1.5 cents from the sale of each quart of milk be earmarked

for the purpose of complying with the regulatory accrual mechanism. That is, the money used to comply with the district court's injunction would be paid by the consumers of milk in Puerto Rico. ORIL also adopted Regulation No. 12, which established that the monies raised from the sale of milk be deposited in a special account within the Milk Industry Development Fund.[1]

The dissent from denial of en banc review argues that the injunction issued by th district court contravenes the strictures of the Eleventh Amendment because it makes the Commonwealth liable for payment of monetary relief. There is no basis in the record for this conclusion. The dissent bases this conclusion on two mistaken assumptions: (1) that the monies raised by the regulatory accrual are public funds and (2) that the Commonwealth is or would be required to expend public funds or resources to compensate Plaintiffs. I write separately to dispel these assumptions and to clarify that the Commonwealth's dignitary and fiscal interests are not implicated in this case as to require this court to conclude that sovereign immunity poses a bar to relief.

The dissent suggests that funds deposited in the Milk Industry Development Fund are considered public funds of the Commonwealth, and that therefore, the monies deposited in the special account should be considered public funds. However, we are dealing in this case with monies paid by consumers of milk which can only be

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[1] The Fund was created to "promot[e] the production, sale, processing and consumption of fresh milk and its byproducts, and . . . any other activity necessary for the advancement of the milk industry." P.R. Laws Ann. tit. 5, § 1099. It is "supported by contributions from milk producers at the rate of one-half (1/2) cent for each quart of milk produced and accepted by the processors for pasteurizing." *Id.*

used for the purposes designated by the injunction. There is no indication that the funds deposited in the special account would be or can be commingled with the Commonwealth's general revenues, or with the monies deposited in the Milk Industry Development Fund according to the law. More importantly, *the Defendants have not argued on appeal that the monies raised by the regulatory accrual are public in nature.* On the basis of the record before us, it is therefore impermissible to suggest, as the dissent does, that the injunction reaches the Commonwealth's funds.

Secondly, there is simply no indication in the record or in the Regulations adopted by ORIL that an eventual judgment ordering disbursal of the monies raised pursuant to the regulatory accrual would be satisfied by public funds or that the Commonwealth's resources would be affected if in due course the Plaintiffs are found entitled to the monies raised by the regulatory accrual.[2] *Neither the Commonwealth nor ORIL have been adjudged responsible for contributing funds to the special account,* and the contributions made to the account are kept separate from the Commonwealth's general revenues and from the Milk Industry Development Fund's monies. Thus, the revenues raised by the regulatory accrual are special funds that do not make the Commonwealth the real party in interest for Eleventh Amend-

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[2] The intricacies of the regulatory mechanism that Defendants adopted have not been challenged by the parties. Defendants have not argued on appeal or in their petition for rehearing en banc, that the regulatory mechanism forces the Commonwealth to expend public funds or resources in violation of the Eleventh Amendment. Therefore, any arguments raised by the dissent *sua sponte* regarding the details of the regulatory accrual are insufficient to justify rehearing in this case.

ment purposes. *See Hudson* v. *City of New Orleans*, 174 F.3d 677, 689 (5th Cir. 1999) (reasoning that, for Eleventh Amendment purposes, the fact that an entity receives state funds which are earmarked for specific or special purposes counsels against finding that the state would be responsible for the entity's debts and obligations); *Brown* v. *Porcher*, 660 F.2d 1001, 1006-07 (4th Cir. 1981) (holding that the Eleventh Amendment posed no bar to compensation payable from South Carolina's unemployment compensation fund which was a special fund "insulated" from public monies and separately financed). *Cf. Austin* v. *Berryman*, 862 F.2d 1050, 1056 (4th Cir. 1988) (holding that the Eleventh Amendment barred monetary relief against Virginia's unemployment compensation fund which was "integrated" into the state's treasury).

The fact that the special account was created within the Milk Industry Development Fund is insufficient to conclude that the Commonwealth would be required to expend state funds to comply with the injunction. The Commonwealth simply has not been required to appropriate *its funds* to comply with the regulatory accrual, and given that the funds deposited in the special account are earmarked to comply with the regulatory mechanism, there is no basis to conclude that a final judgment in favor of Plaintiffs would amount to a judgment against the Commonwealth.[3]

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[3] In fact, the precise compensation that Plaintiffs will be entitled to receive has not been determined as of yet, nor can it be gleaned from the record that the Commonwealth will bear any type of subsidiary monetary liability in this case. Thus, any contention that such an impermissible outcome is within the realm of possibility on the present record, is beyond speculation.

The dissent rightly cautions that the analysis of an entity's entitlement to sovereign immunity should not be transformed into a formalistic inquiry. However, the dissent mistakenly criticizes the panel for engaging in this type of inquiry. Far from adopting a formalistic approach towards Eleventh Amendment analysis, the panel's decision considers, from a practical perspective, the Commonwealth's immediate and ultimate liability and holds that sovereign immunity poses no bar to the relief ordered by the district court, precisely because the Commonwealth was not adjudged liable for payment of a monetary judgment, or held in any fashion subsidiarily responsible for providing the funds that nurture the special account.

Likewise, the dissent errs in asserting that the panel's decision is inconsistent with the Supreme Court's decision in *Regents of the University of California* v. *Doe*, 519 U.S. 425 (1997). In *Doe*, the Supreme Court held that the Eleventh Amendment barred a claim for monetary relief against the State of California, even though the damages would be paid by a third party. For Eleventh Amendment purposes, the Supreme Court found it irrelevant that the State of California had been relieved of its obligation to pay a judgment because a third party would cover the state's liability. In *Doe*, the State of California assumed an obligation upon a finding of liability. In contrast, the district court has never adjudged the Commonwealth liable for monetary relief in this case. Thus, while the Supreme Court clarified in *Doe* that the state's potential legal liability was the relevant factor in the Eleventh Amendment question regardless of the possibility of third-party indemnification, in this case the Commonwealth *has not been held legally or potentially liable* for compensatory damages. That is, the consumers of milk in Puerto Rico are not relieving the Common-

wealth of its liability, since the Commonwealth has not been adjudged liable for the type of compensatory damages that the State of California was potentially liable for in *Doe*.[4] Rather than contravening our panel decision, the Supreme Court's decision in *Doe* supports the conclusion that where there is no basis to find that the state is potentially liable for monetary compensation, the Eleventh Amendment poses no bar to relief, such as the one ordered by the district court in this case.

*Doe* established that the state's legal liability is a crucial consideration in Eleventh Amendment analysis. But that liability is inextricably bound to the overriding question of whether the state would be "legally and practically" required to pay a monetary judgment. *See Hess*, 513 U.S. at 51 (stating, that where "legally and practically" the state would not be required to cover the entity's indebtedness, "the Eleventh Amendment's core concern is not implicated"). In this case, however, it is pure speculation to state that the Commonwealth is legally, practically or potentially bound to expend funds in the event that the monies raised from milk sales prove insufficient to compensate the milk producers. Unlike *Doe* where the State of California was considered to be *potentially liable to plaintiffs*, the Commonwealth's liability in this case is *speculative* in nature. As I have stated, the funds used to comply with the district court's injunction are raised from the price consumers pay for milk and the revenues

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[4] The Supreme Court's decision in *Doe* is distinguishable because it dealt with an indemnification agreement between the State and a third party. This contractual relationship had nothing to do with the relationship between the state and the plaintiff who sought relief against the state in federal court. That is, the presence of third-party indemnitor in *Doe* failed to alter the state's liability towards the plaintiff.

are kept in a special account which is segregated from the Commonwealth's funds. Rather than imposing potential liability on the Commonwealth or its agencies, this regulatory mechanism imposes an obligation on the consumers of milk and carefully shields the Commonwealth's funds and resources from potential liability. Therefore, the dissent's claim that the Commonwealth would be required to pay a monetary judgment is speculative and is insufficient to conclude that the district court's order violates the Eleventh Amendment.

Pursuant to the Supreme Court's decision in *Doe*, the issue of whether a monetary judgment against a state official is enforceable against the state is still a crucial consideration in Eleventh Amendment analysis. 519 U.S. at 430 (explaining that the Court in *Hess* "focused particular attention" on the fact that the states would not have been obligated to pay the judgment). *See, e.g.*, *Fresenius Med. Care Cardiovascular Res. Inc.* v. *P.R. & Caribbean Cardiovascular Ctr. Corp.*, 322 F.3d 56, 65 (1st Cir. 2003) (explaining that the vulnerability of the state's purse is a salient factor in Eleventh Amendment arm-of-the-state analysis and stating that where it is clear that the state's treasury is not at risk, the control exerted by the state over the entity does not entitle the state to immunity); *Metcalf & Eddy, Inc.* v. *Puerto Rico Aqueduct & Sewer Auth.*, 991 F.2d 935, 939 (1st Cir. 1993) ("The Eleventh Amendment's primary concern is to minimize federal courts' involvement in disbursal of the state fisc."). Thus, the panel's opinion is consistent with settled precedent that examines an entity's entitlement to sovereign immunity through the prism of the financial burden actually or potentially imposed on the state.

Finally, the dissent mistakenly contends that the panel's decision ignores the Commonwealth's dignitary interests, which are protected by the Eleventh Amendment. In examining the contours of the state's sovereign immunity, the Supreme Court has explained that the Eleventh Amendment confirms the very essence of the principle of dual sovereignty embedded in the nation's constitutional structure. *Blatchford* v. *Native Vill. of Noatak & Circle Vill.*, 501 U.S. 775, 779 (1991). Though the injunction requires ORIL to adopt the regulatory mechanism, ORIL was not stripped of its power to set the price of milk and to regulate the Milk Industry. Given that ORIL retains control over the milk industry, the panel rightly concluded that the regulatory accrual has not burdened the Commonwealth's entitlement to respect as a sovereign entity in a manner that contravenes the Eleventh Amendment.

In sum, the panel's decision in this case evaluates the substance of the relief afforded by the district court and draws the line against the application of sovereign immunity. This case simply does not involve a monetary award against the state that burdens the state's treasury, nor does it implicate the Commonwealth's dignitary interests in a manner offensive to the Eleventh Amendment. I therefore concur with the majority in denying en banc review.

LYNCH, Chief Judge, dissenting from the denial of en banc review.

With the greatest respect for my colleagues, I disagree with the decision to deny en banc review and think the serious issues raised deserve greater attention from this court and, failing that, from the Supreme Court.

Review en banc is sought by defendant state officials from Puerto Rico's Milk Regulatory Board (Spanish acronym "ORIL"), and the Commonwealth's Secretary of Agriculture, on the ground that the Eleventh Amendment prohibits the remedy ordered by the district court and affirmed by the panel. That remedy was an injunction that forces the Administrator of ORIL, a state administrative agency, to retroactively compensate plaintiffs for the profits they say ORIL deprived them of from 2003 to the time the injunction went into effect in 2007. Under that compulsion the defendant state officials imposed a new surcharge on consumers, the funds from which go into a state-administered public fund and are to be used for the sole purpose of paying plaintiffs for their compensatory damages. Surely this raises significant Eleventh Amendment immunity concerns.

The panel held that there is no Eleventh Amendment bar because the relief took the form of an injunction and the injunction did not force the Commonwealth to satisfy the judgment with funds directly paid from or funneled through the state treasury. That is not, in my view, the appropriate test under the Supreme Court's Eleventh Amendment jurisprudence, and it will lead to federal court orders designed to evade the requirements of the Eleventh Amendment.

I believe the panel has misread *Hess* v. *Port Authority Trans-Hudson Corp.*, 513 U.S. 30 (1994), and has done so in a way which is inconsistent with more than a decade's worth of subsequent Supreme Court precedents, including *Regents of the University of California* v. *Doe*, 519 U.S. 425 (1997), and *Federal Maritime Commission* v. *South Carolina State Ports Authority*, 535 U.S. 743 (2002), as well as our circuit precedent in *Fresenius Medical Care Cardiovascular Resources, Inc.* v. *Puerto*

*Rico and the Caribbean Cardiovascular Center Corp.*, 322 F.3d 56 (2003), and precedent from other circuits. The importance of this issue and its stakes for the states in the many cases in which individuals seek compensation for past constitutional violations make this, in my view, a case warranting en banc review. The issues raised are admittedly difficult, and there is no Supreme Court case directly on point.

## I. Facts

Like many states in the United States, the Commonwealth of Puerto Rico extensively regulates its dairy industry. ORIL, a division of the Puerto Rican Department of Agriculture, is the relevant administrative agency performing this function. Through its regulations, ORIL controls all aspects of the Puerto Rican milk industry. *See generally* J.W. Gruebele and L.F.C. Barahona, *Growth of the Dairy Industry in Puerto Rico*, 14 Illinois Agric. Econ. 32 (1974). Among the ways it does so are by setting the price Puerto Rican consumers pay for processed fresh milk, the margins that all domestic dairy farmers, milk processors, retailers, and distributors receive from the consumer price, and the internal price that milk processors pay to buy raw milk from dairy farmers. *See* P.R. Laws Ann. tit. 5, §§ 1096, 1107.

The plaintiffs, Puerto Rico's two fresh milk processors, brought a civil rights suit under 42 U.S.C. § 1983 against the Administrator of ORIL and the Secretary of Agriculture in their official capacities, claiming that ORIL's pricing scheme was unconstitutionally arbitrary and had, since 2003, deprived them of profits to which they were entitled.[5] Plaintiffs' requested relief included

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[5] Specifically, plaintiffs claimed that since 2003, ORIL had used outdated economic data and had unfairly favored dairy farmers and

"a temporary mechanism for plaintiffs to recover the losses they have experienced on account of the unconstitutional regulation herein under attack."

On July 13, 2007, the federal district court of Puerto Rico held that since 2003, ORIL's price scheme had been violating the Due Process Clause, the Equal Protection Clause, the dormant Commerce Clause, and the Takings Clause of the United States Constitution. *See Vaquería Tres Monjitas* v. *Fabré Laboy*, No. 04-1840 (D.P.R. July 13, 2007). It issued a preliminary injunction which provided in relevant part:

> *The Administrator [of ORIL] is ordered to adopt a temporary mechanism that will allow the processors to recover* the new rate of return they are entitled to (whatever that may be) for the year 2003 (base cost year of the present [price] structure) and up to the day when they begin to recover said rate based on the new regulatory standards and corresponding order. *The Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of his choosing.* The period for this special recovery shall be reasonably determined by the Administrator. The Administrator will hold hearings for this purpose with the participation of plaintiffs, and all parties within the milk industry, within a period of

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other entities at the expense of fresh milk processors when formulating the annual pricing schemes for the milk industry. Plaintiffs claimed they were therefore unable to obtain reasonable profits. They alleged violations of, inter alia, the Due Process Clause, the Equal Protection Clause, and the Takings Clause.

> thirty (30) days of this Opinion and Order. A decision of the Administrator shall follow promptly.

*Id.* at 102 (emphasis added).

The panel depicts the regulatory accrual mechanism ORIL adopted pursuant to this injunction as an informal remedy that would not require any state action beyond the initial price order and would not be collected or retained by the Commonwealth. *See Vaquería Tres Monjitas*, 587 F.3d at 479. The facts do not support that characterization. ORIL promulgated the regulatory accrual mechanism through a formal regulation and administrative order subject to Puerto Rico's Uniform Administrative Procedure Act, P.R. Laws Ann. tit. 3, § 2121 *et seq.* Like a tax, the mechanism raises revenue through a method available only to sovereigns. It also entails extensive state involvement well beyond the promulgation of the initial price order.

The regulatory accrual mechanism works as follows. On April 17, 2008, after nine months and 375 docket entries' worth of further litigation over the terms of the injunction, ORIL issued a regulation and administrative order setting forth the details of the mechanism. The regulation created a special fund (called "the reserve for the eventual compensation for losses caused to the processing plants by the previous regulations") out of which plaintiffs' past losses were to be paid. ORIL did this by adding the regulatory accrual as one of the costs to be included in determining the new price of milk that consumers would pay in Puerto Rico. "This contribution for the abovementioned compensation," the regulation continued, "shall be retained and deposited in a special account in the Milk Industry Development Fund, which

will keep and manage the special account in compliance with the orders it receives from the administrator of [ORIL]."[6]

In an accompanying administrative order, ORIL also set a new price structure for the consumer price of fresh milk in Puerto Rico.[7] Originally, ORIL, pursuant to an agreement with plaintiffs, determined that 1.25 cents from every quart of milk sold to consumers would go into the special account for plaintiffs' compensation. A July 22, 2008 ORIL regulation increased that amount to 1.50 cents per quart. Under compulsion of the injunction, in August 2008, ORIL and plaintiffs also agreed that plaintiffs would be compensated out of the fund for their past damages from December 31, 2002 to December 31, 2007, but did not reach the issue of prospective compensation for 2008. These regulations and administrative orders were subject to the formal requirements of Puerto Rico's Uniform Administrative Procedure Act, including a notice and comment period.

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[6] The Milk Industry Development Fund (Spanish acronym "FFIL") was established to promote the fresh milk industry. It is administered by an Administrative Board chaired by the Administrator of ORIL, and by law, "[a]ll monies in the Fund . . . shall be acknowledged as depositories of funds of the Commonwealth of Puerto Rico, but they shall be kept in an account or accounts under the name of the Fund." P.R. Gen. Laws. Ann. tit. 5, § 1099(e). Thus, Puerto Rican law characterizes the funds in the account as funds of the Commonwealth of Puerto Rico.

[7] Specifically, the new price structure set the consumer price of fresh milk in Puerto Rico ($1.32) and divided the revenues per quart among retailers ($0.09), distributors ($0.02), fresh milk processors ($0.39), dairy farmers ($0.805), the new cost to ORIL of "future audits and regulatory activities" ($0.0025), and the special account contribution for regulatory accrual ($0.0125).

## II. Legal Analysis

When a state official is sued in his or her official capacity but the state is the true party in interest, the suit is barred under the Eleventh Amendment and the state cannot be subject to such a suit without its consent. *See Edelman* v. *Jordan*, 415 U.S. 651, 663 (1974). "Relief that in essence serves to compensate a party injured in the past by an action of a state official in his official capacity that was illegal under federal law" is a classic example of what the Eleventh Amendment prohibits. *Papasan* v. *Allain*, 478 U.S. 265, 278 (1986). This is so irrespective of whether "the relief is expressly denominated as damages." *Id.* "[I]f the relief is tantamount to an award of damages for a past violation of federal law, even though styled as something else," the Eleventh Amendment prohibits it. *Id.*

There can be no doubt that the injunction at issue makes the Commonwealth, through one of its administrative agencies, liable for retrospective monetary relief. By its terms, the injunction is directed against the Administrator of ORIL, an administrative agency within the Department of Agriculture that Puerto Rico has clearly structured as an arm of the state. *See Fresenius*, 322 F.3d at 65. It is equally clear that the regulatory accrual compelled by the injunction is retrospective, not prospective.[8] Plaintiffs, the district court, and subse-

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[8] The district court clearly erred when it characterized the relief as "prospective injunctive relief against the Defendants to avoid insolvency" as opposed to retrospective compensatory relief. *See Vaquería Tres Monjitas*, No. 04-1840, slip op. at 13-14 (D.P.R. Oct. 2, 2006) (order denying motions to dismiss). Plaintiffs say the regulatory accrual is really prospective because its purpose is to rebuild plaintiffs' capital base and no pricing structure, going forward, would be effective without this step. But that argument would open the floodgates to retrospective compensation in almost any situation.

quent ORIL regulations implementing the injunction have all characterized the regulatory accrual as a way to allow plaintiffs to recover the *past* profits they say they lost between 2003 and the time of the injunction. It appears indistinguishable from "the award, as continuing income rather than as a lump sum, of an accrued monetary liability," which the Supreme Court has long characterized as retrospective monetary relief barred by the Eleventh Amendment. *Papasan*, 478 U.S. at 281 (internal quotation marks and emphasis omitted); *Edelman*, 415 U.S. at 668 (holding that payment of state funds as compensation to plaintiffs whose benefits were delayed by slow processing times was "indistinguishable in many aspects from an award of damages against the State"); *see also Whalen* v. *Mass. Trial Court*, 397 F.3d 19, 29-30 (1st Cir. 2005) (holding that the restoration of service credit following past termination is impermissible retrospective compensation); *Fla. Ass'n of Rehab. Facilities, Inc.* v. *Fla. Dep't of Health & Rehab. Servs.*, 225 F.3d 1208, 1220-21 (11th Cir. 2000) (holding that an injunction "to prescribe a set of standards upon which Defendants are to provide reimbursement for inadequate past and future payments" is barred).

The panel opinion nonetheless held that the Eleventh Amendment is not an issue because the "state treasury" is not involved.[9] That conclusion, to my mind, is doubtful.

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The panel opinion assumed this relief was retrospective and rested its holding on the theory that retroactive compensatory relief that does not come directly from the state treasury does not violate the Eleventh Amendment. *Vaquería Tres Monjitas*, 587 F.3d at 478.

[9] Plaintiffs suggest in the alternative that *First English Evangelical Lutheran Church* v. *County of Los Angeles*, 482 U.S. 304, (1987), held, and our caselaw supports, the proposition that retroactive compensation for a Takings Clause claim is an exception to the Eleventh Amendment's usual bar on retrospective relief. The panel opi-

First, the conclusion assumes that if third parties — here, consumers — provide the funds the Commonwealth uses to compensate plaintiffs and the payments are not made directly out of the state treasury, the state's Eleventh Amendment interests are not involved. Second, the conclusion assumes that payments from an administrative fund created and maintained as public funds do not involve the state's fisc.

Third, the panel opinion, in my view, most likely departs from precedent when it holds that the Eleventh

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nion rests instead on the ground that the regulatory accrual was an equitable remedy because there was no formal award of damages. *Vaquería Tres Monjitas*, 587 F.3d at 479-80.

Plaintiffs' position misinterprets the holdings of *Parella* v. *Retirement Board of Rhode Island Employees' Retirement System*, 173 F.3d 46 (1st Cir. 1999), and *Tenoco Oil Co., Inc.* v. *Department of Consumer Affairs*, 876 F.2d 1013 (1st Cir. 1989). *Parella* did not hold that the Eleventh Amendment allows the recovery of just compensation for temporary takings despite its retrospective nature. It was instead concerned with the complications such a position could pose for courts if *Steel Co.* v. *Citizens for a Better Environment*, 523 U.S. 83, (1998), were interpreted to require courts to reach Eleventh Amendment questions before other dispositive issues. 173 F.3d at 56-57. *Tenoco* mentioned *First English* only in passing and disposed of the case on the ground that permanent injunctions should not be imposed prior to final administrative actions. 876 F.2d at 1028-29.

In any event, *First English* did not squarely present an Eleventh Amendment question, since it involved a suit against a county, which cannot invoke Eleventh Amendment immunity. 482 U.S. at 308. And in the analogous context of compensation for reverse condemnation claims, we have stated that the Eleventh Amendment bars federal courts from granting this relief. *See Citadel Corp.* v. *P.R. Highway Auth.*, 695 F.2d 31, 33 n.4 (1st Cir. 1982); *see also Seven Up Pete Venture* v. *Schweitzer*, 523 F.3d 948, 954-56 (9th Cir. 2008) (holding that the Eleventh Amendment bars retroactive compensation both under the Takings Clause and for reverse condemnation claims under the Due Process Clause).

Amendment is not involved when the Commonwealth is ordered to raise money from individuals through mechanisms other than a general tax that produces funds for the state treasury. This provides an easy mechanism for evasion of the Eleventh Amendment. A key purpose of the Eleventh Amendment is to protect the state's dignitary interests in how it chooses to impose surcharges, fees, and alternatives to taxation to provide funds for public purposes.

Whether an action in practice aims to recover money from a state, in violation of the Eleventh Amendment, is a functional question, and *Regents of the University of California* v. *Doe*, 519 U.S. 425 (1997), expressly rejected the argument that Eleventh Amendment immunity turns upon "a formalistic question of ultimate financial liability." *Id.* at 431. Instead, "it is the entity's potential legal liability, rather than its ability or inability to require a third party to reimburse it, or to discharge the liability in the first instance, that is relevant." *Id.*

Thus, *Doe* held that the Eleventh Amendment barred a suit against the University of California, an arm of the state, that made the entity legally liable for compensatory relief even though the judgment would not, in practice, be paid by the state because of an indemnity arrangement.[10] *Id.* at 426. Perhaps *Doe* is no more than a

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[10] Another circuit, applying *Doe*, has rejected the claim that the Eleventh Amendment is not implicated so long as a judgment against a state does not require any new expenditures from the state treasury. "[T]he proper inquiry is not whether the state treasury would be liable in *this* case, but whether, hypothetically speaking, the state treasury would be subject to 'potential legal liability' *if* the [source in question] did not have the money to cover the judgment." *Ernst* v. *Rising*, 427 F.3d 351, 362 (6th Cir. 2005) (en banc). The panel opinion puts our circuit in conflict with the Sixth Circuit.

variation on the usual collateral source rule, but I am doubtful it is so limited.

The injunction orders the Administrator of ORIL to use the state's regulatory, revenue-raising powers to satisfy plaintiffs' demand for compensation for lost profits from 2003 to the time of the injunction, and ORIL adopted the regulatory accrual mechanism to comply with the injunction. The only reason this mechanism exists is to recover enough money so that plaintiffs get four years' worth of past lost profits. The mechanism is an option ORIL can use to satisfy the judgment only because the Commonwealth's powers over the milk industry in Puerto Rico are so extensive. The fact that the payments may not already have been made is irrelevant. And if this mechanism failed — if, for instance, consumers bought less fresh milk in response to the raised prices and the regulatory accrual failed to accumulate the significant sums needed to repay plaintiffs — there is no indication ORIL would not still be on the hook for plaintiffs' lost profits. The prospect of such liability may well be enough to make the Eleventh Amendment a shield. *See Doe*, 519 U.S. at 431,; *see also Fed. Maritime Comm'n.*, 535 U.S. at 766-67.

When a state raises revenues through the methods available to it as a sovereign — including taxation and regulatory orders — rather than by withdrawing existing funds in the state treasury, this surely does not remove the Eleventh Amendment's protections. Either way, the state fisc is affected because the state is being required "to use its own resources" to replace the original source of the plaintiffs' profits. *Papasan*, 478 U.S. at 281. The regulatory accrual ORIL has adopted under compulsion by the district court essentially imposes a tax on Puerto Rican consumers: it increases the overall price

of milk to consumers and channels 1.50 cents from every quart to compensate the plaintiffs for their lost profits. ORIL then sequesters this money in an account in the FFIL, not unlike the way tax revenues are collected.[11] The fact that the special account in the FFIL was created to comply with the injunction and that the money in the account was never previously held by the state is irrelevant. "Where [the state] gets the money to satisfy a judgment is no concern of the plaintiff or the court; what matters is that the judgment runs against the state." *Paschal v. Jackson*, 936 F.2d 940, 944 (7th Cir. 1991) (internal quotation marks omitted).

Moreover, the injunction does force the Commonwealth to expend funds from its own public funds to pay plaintiffs' lost profits.[12] Under the regulatory accrual mechanism, the money collected from consumers goes into a special account in the FFIL that is controlled and admi-

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[11] Indeed, the regulatory accrual mechanism here functions similarly to the pricing scheme Massachusetts imposed to charge milk dealers additional money for the benefit of in-state dairy farmers in *West Lynn Creamery, Inc.* v. *Healy*, 512 U.S. 186, (1994). Under that mechanism, Massachusetts, which at the time exercised considerable regulatory control over in-state milk prices, ordered every milk dealer operating in Massachusetts to make a monthly payment into the "Massachusetts Dairy Equalization Fund," a special account, which was then distributed to Massachusetts producers every month. *Id.* at 190-91. The Supreme Court described this pricing scheme as "effectively a tax." *Id.* at 194.

[12] Defendants' Eleventh Amendment argument on appeal rested on the theory that the regulatory accrual effectively made ORIL, an arm of the state, liable for retroactive compensation. Under defendants' theory, these funds were by definition state funds, and the issue of whether the regulatory accrual implicates the state treasury is therefore before us. In any event, questions of Eleventh Amendment immunity can be raised by this court sua sponte, *see Parella*, 173 F.3d at 55.

nistered by ORIL for eventual disbursal to plaintiffs. And all monies stored in the FFIL are, as a matter of Puerto Rican law, considered depositories of the Commonwealth. This is plainly relief that reaches the state fisc.

The fact that this is a special fund and not intermingled with the Commonwealth's general revenues does not remove Eleventh Amendment scrutiny. Reliance on this fact again elevates form over substantive reality. *Doe* certainly suggests that this kind of distinction is irrelevant. Even before *Doe*, the Supreme Court had long suggested that the definition of a state "treasury" includes segregated funds held in special accounts, not just the state's general revenue accounts. *See, e.g., Kennecott Copper Corp.* v. *State Tax Comm'n*, 327 U.S. 573, 576 (1946); *Great N. Life Ins. Co.* v. *Read*, 322 U.S. 47, 52-53 (1944); *see also Esparza* v. *Valdez*, 862 F.2d 788, 794 (10th Cir. 1988). This is so even if the source of the funds came from third parties like the federal government and not from an existing pool of state money. *See, e.g., Paschal*, 936 F.2d at 944. Practical considerations also favor this approach. Defining the state's "treasury" to mean money in a state's general revenues account and not elsewhere would turn the Eleventh Amendment into an exercise in forensic accounting. I admit that this case may be viewed as another example of a "spectrum" problem. What is involved is not a tax but an administrative surcharge. But the Court, understandably, has preferred harder, bright line rules.

The panel's legal analysis of the Eleventh Amendment issue also seems to me to ignore another state interest the Supreme Court has identified. The Court has held that a single-minded focus on whether relief comes directly from the state treasury or otherwise threatens

states' financial welfare "reflects a fundamental misunderstanding of the purposes of sovereign immunity." *Fed. Maritime Comm'n*, 535 U.S. at 765. The Eleventh Amendment "serves the important function of shielding state treasuries," but "the doctrine's central purpose is to accord the States the respect owed them as joint sovereigns," and that broader concern must inform the analysis.[13] *Id.* (internal quotation marks omitted); *see also id.* at 760.

My concern is not with some collection of vague interests which might be labeled "dignitary" interests. It is plain that the power to tax — and presumably analogous regulatory means of raising revenue — is "central to state sovereignty." *See Dep't of Revenue* v. *ACF Indus., Inc.*, 510 U.S. 332, 345 (1994). Surely we must consider whether these interests are offended when a district court orders state officials to enact an elaborate regulatory scheme that imposes surcharges, special fees, or user fees in order to raise and pay out money in damages rather than simply withdrawing plaintiffs' retroactive compensation from the state treasury. If courts can

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[13] This is not to say that our inquiry must swing to a single-minded focus only on whether a given suit offends a state's dignitary interests. As the Supreme Court clarified in *Verizon Maryland, Inc.* v. *Public Service Commission of Maryland*, 535 U.S. 635 (2002), whether a suit can proceed under *Ex Parte Young* turns on "a straightforward inquiry into whether [the] complaint alleges an ongoing violation of federal law and seeks relief properly characterized as prospective." *Id.* at 645 (alteration in original) (internal quotation marks omitted). But as other circuits have concluded, the state's sovereign interests are still relevant to the analysis and should not be ignored. *See, e.g., Virginia* v. *Reinhard*, 568 F.3d 110, 119-21 (4th Cir. 2009) (considering whether the state's "special sovereign interests" would be implicated in an *Ex Parte Young* action by a state administrative agency against state officials); *Union Elec. Co.* v. *Mo. Dep't of Conservation*, 366 F.3d 655, 658 (8th Cir. 2004).

evade Eleventh Amendment constraints by dictating to states that they find ways in which state officials can use the state's regulatory money-raising powers to satisfy a money judgment, the Eleventh Amendment's bar against retrospective monetary relief becomes a nullity.

My concerns are raised against the backdrop that the Court's refashioning of the interests at stake under the Eleventh Amendment has, in the wake of *Doe* and *Federal Maritime Commission*, reshaped the test for when an entity is an arm of the state. *See Fresenius*, 322 F.3d at 63, 67-68 (holding that the arm-of-the-state inquiry depends on a multi-factor test beginning with the way the state structures an entity and does not rely exclusively on whether damages against the entity would be paid from the state treasury); *see also Cooper* v. *Se. Penn. Transp. Auth.*, 548 F.3d 296, 301 (3d Cir. 2008) ("In light of *Doe* and *FMC*, we held that we can no longer ascribe primary to the [state-treasury] factor in our sovereign immunity analysis.") (alteration in original) (internal quotation marks omitted). We must face up to the way these transformations in Eleventh Amendment doctrine also affect the underlying immunity question.

For these reasons, I respectfully dissent from the denial of en banc review.

## APPENDIX C

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF PUERTO RICO

No. 04-1840

VAQUERÍA TRES MONJITAS, INC., and SUIZA DAIRY, INC.,
Plaintiffs,

*v.*

JOSE O. FABRE LABOY, in his official capacity as Secretary of Agriculture of the Commonwealth of Puerto Rico, and JUAN R. PEDRÓ-GORDIÁN, in his official capacity as Administrator of the Milk Industry Regulatory Office of the Commonwealth of Puerto Rico,
Defendants.

July 13, 2007

## AMENDED OPINION AND ORDER GRANTING PRELIMINARY INJUNCTION

DOMINGUEZ, District Judge. This matter came on to be heard on a complaint filed by plaintiffs on August

13, 2004. [Dkt. No. 1][1] Plaintiffs, fresh milk processors, attacked as unconstitutional certain critical aspects of the regulation of the milk market by the Government of the Commonwealth of Puerto Rico. The complaint and its amendments seek declaratory and injunctive relief. The petition for a preliminary injunction under Fed. R. Civ. P. 65 was filed on August 20, 2004 [Dkt. No. 2] and seeks an order precluding the Administrator of the Milk Industry Regulatory Office (by its Spanish acronym "ORIL") from continuing to implement certain decisions that plaintiffs claim are unconstitutional. Plaintiffs, Vaqueria Tres Monjitas, Inc. (Tres Monjitas) and Suiza Dairy, Inc. (Suiza) challenge the constitutionality, as implemented, of the laws and regulations that govern the milk industry in Puerto Rico, particularly the Milk Industry Regulation Act No. 34 of June 11, 1957, 5 P.R. Laws Ann. § 1092-1125 (Act 34) and Regulation No. 1 of June 11, 1957 (Milk Regulation No. 1) as subsequently amended, all under Due Process, Equal Protection, the Takings Clause and, finally, the Dormant Commerce Clause.

Because of the sensitive nature of a constitutional attack on a heavily regulated market, the court held numerous days of hearings and received copious evidence. Fifty-one preliminary injunction hearings were held between February 15, 2005 and August 5, 2006.[2] The hear-

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[1] The complaint was amended on two occasions. The Amended Complaint was filed on June 13, 2005 (Dkt. No. 143). Second Amended Complaint was filed upon request of this court based on representations by defendants on September 14, 2005 (Docket. No. 206-1).

[2] The undersigned presided over forty-nine (49) of the fifty-one (51) evidentiary hearings held by the court. The first two (2) hearings were presided over by then Magistrate Judge Aida Delgado after Magistrate Judge Justo Arenas disqualified himself "sua sponte". (Docket No. 27) Magistrate Judge Aida Delgado presided over the

ings were held not only with the participation of plaintiffs and the Government officers in charge of implementing the milk regulations, but also with the participation of interveners Indulac and the Association of Dairy Farmers all of whom are affected/favored by the challenged laws and regulations as later explained in this Opinion and Order.

In addition to presenting evidence, the parties have submitted detailed memorandums of law after the last hearing held on August 5, 2006. The court further granted the parties the reasonable time requested to file memorandums and corresponding oppositions, replies and sur-replies which were all filed by January 3, 2007. Oral arguments were heard on February 7, 2007. Motions containing exhibits to update the record have been filed by the parties.

Subsequently the parties have supplemented the record as the challenged actions continue to occur. Now, having heard and considered the motions, evidence, memorandums and arguments this court is ready to rule. A preliminary injunction is issued for the reasons stated herein.

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hearings upon order of District Judge Carmen C. Cerezo. (Docket No. 45) Magistrate Judge Aida Delgado recused herself "sua sponte". (Docket No. 70) The case was reassigned to then Magistrate Judge Gustavo Gelpi. (Docket No. 74) Shortly thereafter, District Judge Carmen C. Cerezo recused herself "sua sponte" as well. (Docket No. 76) The case was then referred to District Judge Perez Gimenez, who also recused himself "sua sponte". Finally the case was assigned to the docket of the undersigned. (Docket Nos. 77, 78 and 79)

## STANDARDS FOR PRELIMINARY INJUNCTION IN THE FIRST CIRCUIT

Because injunctive relief has been requested, before setting the factual scenario in the instant case, the court reviews the basic injunctive standard applicable in the First Circuit Court.

For injunctive relief to be issued under Fed.R.Civ.P. 65, the party seeking the preliminary injunction remedy must establish that: (1) it is substantially likely to prevail on the merits of the claim; (2) absent the injunction there is a significant risk of irreparable harm; (3) the balance of hardships weights in its favor; and (4) the injunction will not harm public interest. *See New Comm. Wireless Servs., Inc. v. SprintCom, Inc.*, 287 F.3d 1, 8-9 (1st Cir. 2002). The First Circuit has instructed the trial courts to use the aforementioned quadripartite test when considering requests for preliminary injunctions. *See Narragansett Indian Tribe v. Guilbert*, 934 F.2d 4, 5 (1st Cir. 1991).

### A. Likelihood of Success on the Merits

As to the first factor, likelihood of success, the First Circuit has stated, **"Our analysis begins with probability of success, as we have often found this furcula to be critical."** Id., at 6 *(emphasis added).* See also, *Public Service Co. v. West Newbury*, 835 F.2d 380, 383 (1st Cir. 1987); *Lancor v. Lebannon Housing Auth.*, 760 F.2d 361, 362 (1st Cir. 1985) ("Of these four factors, the probability-of-success component in the past has been regarded by us **as critical** in determining the propriety of injunctive relief"); *Planned Parenthood League v. Bellotti*, 641 F.2d 1006, 1009-22 (1st Cir. 1981). (Emphasis ours.)

In the same vein, the overseeing appellate court has called the likelihood of success factor the **"sine qua non"** of the preliminary injunction test.[3] "The sine qua non of that formulation is whether the plaintiffs are likely to succeed on the merits. In the ordinary course, plaintiffs who are unable to convince the trial court that they will probably succeed on the merits will not obtain interim injunctive relief." *See Weaver v. Henderson*, 984 F.2d 11, 12 (1st Cir. 1993); *see also, SEC v. Fife*, 311 F.3d 1, 8 (1st Cir. 2002); *New Comm. Wireless Servs. Inc. v. Sprintcom, Inc.* 287 F.3d 1, 9 (1st Cir. 2002) ("The sine qua non of this four-part inquiry is likelihood of success on the merits: if the moving party cannot demonstrate that he is likely to succeed in his quest, the remaining factors become matters of idle curiosity.") *Auburn News Co. v. Providence Journal Co.*, 659 F.2d 273, 277 (1st Cir. 1981) ("[T]he probability-of-success component has loomed large in cases before this court."), cert. denied, 455 U.S. 921, 102 S. Ct. 1277, 71 L.Ed.2d 461 (1982); *LeBeau v. Spirito*, 703 F.2d 639, 645 (1st Cir. 1983) (affirming denial of preliminary injunction and ending inquiry after concluding that plaintiffs were unlikely to prevail on the merits).

The First Circuit has further stated, "[t]he heart of this test is . . . the question whether the harm caused plaintiff without the injunction, in light of the plaintiff's likelihood of eventual success on the merits, outweighs the harm the injunction will cause defendants." *Vargas-Figueroa v. Saldana*, 826 F.2d 160, 162 (1st Cir. 1987); *see also, Massachusetts v. Watt*, 716 F.2d 946, 953 (1st Cir. 1983); *SEC v. World Radio Mission*, 544 F.2d 535,

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[3] ***Sine qua non:*** Without which not. That without which the thing cannot be. An indispensable requisite or condition. *Black's Law Dictionary*, 1990.

541-42 (1st Cir. 1976) ("To the extent that a defendant can show harm, this must be discounted by the degree that a plaintiff can show likelihood of success. The more foreseeable is the plaintiff's ultimate success, the less weight is to be given to the defendant's prospective loss.").

**B. Irreparable Harm**

This criteria "must not be assumed, it must be demonstrated . . . speculative injury does not constitute a showing of irreparable harm". *Narragansett Indian Tribe v. Guilbert*, 934 F.2d at 6, 7 (citations omitted). However, "[a] deprivation of a [federal] constitutional right 'for even minimal periods of time, unquestionably constitutes irreparable injury." *DeNovellis v. Shalala*, 135 F.3d 58, 71-72 (1st Cir. 1998); *see also Justino Acevedo-Luis v. Mercedes Pagan*, 478 F. 3d 35, 38 (1st Cir. 2007) ("[t]he loss of First Amendment freedoms, for even minimal periods of time, unquestionably constitutes irreparable injury.") (*emphasis on original*)[4] (*citing Elrod*

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[4] The Court deems necessary to clarify that although in Justino Acevedo-Luis v. Mercedes Pagan, 478 F. 3d at 38, the First Circuit Court of Appeals stated that "'[t]he loss of First Amendment freedoms, for even minimal periods of time, unquestionably constitutes irreparable injury'", this does not help a jury in determining the compensatory damages for redressing a First Amendment violation. The First Circuit went on to clarify that "while the language accurately described one of the requirements for a **preliminary injunction** in a First Amendment case, [ ]it would not be helpful to a jury in determining the compensatory **damages** for a First Amendment violation. Id. (Emphasis on original.) The quoted language, however, is originally from the case of *Elrod v. Burns*, 427 U.S. 347, 373 (1976) which the First Circuit recognizes at *Justino Acevedo*. Notwithstanding the constitutional violations in the instant case as to Due Process, Equal Protection and Takings are from at least 2003 and are more than "for minimal periods of time."

*v. Burns*, 427 U.S. 347, 373, 96 S.Ct. at 2673, 2689-90 (1976); *New York Times Co, v. United States*, 403 U.S. 713, 91 S. Ct. 2140, 29 L.Ed. 2d 822 (1971).

Only a viable threat of serious harm which cannot be undone authorizes exercise of a court's equitable power to enjoin before the merits are fully determined. *Parks v. Dunlop*, 517 F.2d 785 (5th Cir. 1975). A preliminary injunction will not be issued simply to prevent a mere possibility of injury. A presently existing, actual threat must be shown. 11 C. Wright and A. Miller, Federal Practice and Procedure, §2948; *see also State of New York v. Nuclear Regulatory Commission*, 550 F.2d 745 (2nd Cir. 1977); *Crowther v. Seaborg*, 415 F.2d 437 (10th Cir. 1969). However, even under traditional Rule 65 standards, a temporary loss of income which may be recovered later does not usually constitute irreparable injury. *Gately v. Massachusetts*, 2 F.3d 1221, 1232 (1st Cir. 1993). Finally,

> [a] preliminary injunction should not [be] issue[d] except to prevent a real threat of harm. *Ross-Simons*, 102 F.3d at 19; 11A Charles Alan Wright, Arthur R. Miller, & Mary Kay Kane, *Federal Practice & Procedure* § 2948.1, at 153-54 (2d ed.1995). A threat that is either unlikely to materialize or purely theoretical will not do. *Ross-Simons*, 102 F.3d at 19; *Pub. Serv. Co. v. Town of W. Newbury*, 835 F.2d 380, 382 (1st Cir. 1987). An imminent threat that evidence will be lost is one thing — but a claimed threat, unaccompanied by any showing of reasonable grounds for believing that the evidence in question is imperilled, is insufficient to warrant the entry of

> a prophylactic injunction. *Humble Oil & Ref. Co. v. Harang*, 262 F.Supp. 39, 42-43 (E.D.La.1966). **Preliminary injunctions are strong medicine, and they should not [be] issue[d] merely to calm the imaginings of the movant.**

*Matos ex rel. Matos v. Clinton School District*, 367 F.3d 68, 73 (1st Cir. 2004) (*emphasis ours*).

In the instant case violations of Due Process rationality requirements, Equal Protection, acts constituting a taking of property under the Taking Clause and a violation of the Dormant Clause are alleged. The court is of the opinion that should the case pass muster, injunctive relief is in order due to the irreparable harm criteria. *See Tenoco Oil Co., Inc. v. Department of Consumer Affairs*, 876 F.2d 1013 (1st Cir. 1989) (granting injunctive relief under Due Process, Equal Protection and Taking Clause); *Walgreen Co. v. Rullan*, 405 F.3d 50 (1st Cir. 2005) (warranting injunctive relief under the Dormant Commerce Clause).

**C. Balancing of the Relevant Equities**

This criteria requires the court to examine, performing a balancing, on which side do equity lies. "[T]he heart of the matter is whether 'the harm caused plaintiff without the injunction, in the light of the plaintiff's likelihood of eventual success on the merits, outweighs the harm the injunction will cause the defendants'." *See DeNovellis*, 135 F.3d at 77. In other words, the court should focus upon the hardship to the movant if an injunction does not issue as contrasted with the hardship to the nonmovant if it does, and the effect of the court's action on the public interest. *See Matos ex rel. Matos*, 367 F.3d at 73 *(citations omitted)*. Finally, this criteria is the result of a

comparison between the injury suffered by plaintiff outweighing any harm which granting injunctive relief would inflict on the defendant. *Planned Parenthood League*, 641 F.2d at 1009.

### D. The Effect on the Public Interest of a Grant or a Denial of the Restrainer

This criteria requires the Court to weigh where do the public interest lies by the granting or the denial of the injunctive relief. It constitutes a balancing of interest between the granting or the denial based on public interest. The effect on the public interest is measured by whether the public interest would be better served by issuing rather than by denying the injunction. *Massachusetts Coalition of Citizens with Disabilities, et al. v. Civil Defense Agency and Office Emergency Preparedness*, 649 F.2d 71, 74 (1st Cir. 1981).

## FINDINGS OF FACTS

This court specifically finds the following facts proven:[5]

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[5] The court has included public policy facts that the court does not challenge. The court does not question any "political" motives, nor does the court wishes to "sit as a super legislature to weight the wisdom of the Legislature." *Tenoco Oil Co. Inc. v. Department of Consumer Affairs*, 876 F.2d 1013, 1021 (1st Cir. 1989) (internal citations omitted). These facts are included only to provide the reader the benefit of a fuller record enabling a deeper comprehension of the constitutional challenge as to the laws and regulations as applied under Due Process, Equal Protection, the Takings Clause and the Dormant Commerce Clause of the Constitution. The court only challenges the law as applied as it may transgress the Due Process, Equal Protection, Takings Clause and/or the Dormant Commerce Clause.

1. ORIL is an administrative office attached to the Department of Agriculture of Puerto Rico. The Secretary of Agriculture is the head of said Department.[6] ORIL is statutorily empowered to regulate all aspects of the Puerto Rican milk market.[7]

2. The Administrator of ORIL is also the Chairman of the Board of the *Fondo de Fomento de la Industria Lechera* ("FFIL")[8], an entity created by law which is the sole owner of intervener Indulac.[9] Up until after this case was initiated, the Administrator of ORIL was also the Chairman of the Board of Directors of Indulac.[10] As of today, he continues as a member of said board.[11] The FFIL is designed

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[6] See Act 34 of June 11, 1957, P.R. Laws Ann. Title 5 §§ 1092 to 1118, as amended ("Act 34"). All future references to Act 34 are made indicating the P.R. Laws Ann. Title 5 § number, unless otherwise noted. P.R. Laws Ann. § 1093 and 1099(e).

[7] See Legislative History and Declaration of Purpose, as well as the text of Act 34, P.R. Laws Ann. Title 5 § 1092, et seq. approved June 11, 1957.

[8] See Transcript of the Hearing held on November 1, 2005 p. 36 lines 20-24; P.R. Laws Ann. Title 5 § 1099 (e).

[9] See Plaintiff's Exhibit 22 § 4(a) and Plaintiff's Exhibit 57 Art. 2; Transcript of the Hearing held on October 24, 2005, p. 116 lines 6-7; Transcript of the Hearing held on October 25, 2005, p. 10 lines 9-10; Transcript of the Hearing held on November 1, 2005, p. 20 lines 9-11; Transcript of the Hearing held on February 15, 2005, p. 23 line 13-18.

[10] See Transcript of the Hearing held on February 28, 2006, p. 21 lines 7-9; p. 63, line 11 - p. 67 line 1.

[11] See Plaintiff's Exhibit 69, Art. 3, § 1 (a); Transcript of the Hearing held on February 28, 2006, p. 67 line 5 - p. 69 line 8.

and required to promote the consumption of fresh milk.[12]

3. Both the FFIL and Indulac are entities under the full control of the dairy farmers.[13] The FFIL pays for ORIL's Administrator's automobile and other expenses.[14]

4. Indulac, ORIL and the FFIL share among themselves the same building facility.[15] Mr. Jose Benitez, a former dairy farmer is the Chief Executive Officer of the FFIL and also the Chief Executive Officer of Indulac.[16] Mr. Benitez' compensation derives from the FFIL.[17]

5. Mr. Luis Fullana, another dairy farmer and fact and expert lay witness for ORIL is one of the former Administrators of ORIL.[18]

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[12] See Transcript of the Hearing held on October 24, 2005, p. 44 lines 2-8.

[13] See P.R. Laws Ann. Title 5 § 1099(e); Transcript of the Hearing held on February 28, 2006, p. 72 lines 15-17; Transcript of the Hearing held on March 2, 2006, p. 19 lines 15-20.

[14] See Transcript of the Hearing held on February 28, 2006, p. 16 line 16 - p. 18 line 6.

[15] See Transcript of the Hearing held on February 28, 2005, p. 48 line 18 - p. 49 line 1.

[16] See Transcript of the Hearing held on June 5, 2006 p. 69 line 2 - p. 70 line 10.

[17] See Transcript of the Hearing held on June 16, 2006 p. 35 lines 7-8; see also Transcript of the Hearing held on February 15, 2005, p. 29 lines 11-17.

[18] See Transcript of the Hearing held on October 18, 2005, p. 18 line 7 - p. 19 line 5.

6. Indulac is the only entity authorized in Puerto Rico to manufacture UHT milk, a kind of fluid milk that needs no refrigeration prior to opening.[19] Indulac sells locally manufactured UHT under sixteen different private brands. Indulac devotes, by far, most its raw milk to the manufacture of UHT.[20] At all times of the hearings Indulac was in control of approximately 70% of the UHT market in Puerto Rico.[21] The rest of the UHT market belongs to out-of-state producers.[22]

7. Fresh milk and UHT (two forms of fluid milk) are at least imperfect substitutes.[23] When the price of one of those products goes up the quantity demanded for the same goes down and demand for the other product rises accordingly.[24] Fresh milk

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[19] See Transcript of the Hearing held on August 22, 2005, p. 23 lines 4-7; p. 58 lines 2-3.

[20] See Transcript of the Hearing held on March 1, 2006, p. 27 lines 12-21; See also Transcript of the Hearing held on March 2, 2006, p. 17 line 23 - p. 18 line 5.

[21] See Plaintiff's Exhibits 24 and 25 and Defendant's Exhibit KK; See also Transcript of the Hearing held on August 22, 2005, p. 27 lines 14-15.

[22] Id.

[23] See Transcript of the Hearing held on August 22, 2005, p. 45 lines 7-8; Transcript of the Hearing held on September 16, 2005, p. 39 lines 23-25; Transcript of the Hearing held on February 16, 2005, p. 429 lines 13-15; Transcript of the Hearing held on July 6, 2005, p. 121 lines 24-25; Transcript of the Hearing held on July 7, 2005, p. 33 lines 23-24; Transcript of the Hearing held on July 26, 2006, p. 110 lines 21-22.

[24] See Transcript of the Hearing held on August 22, 2005, p. 44 lines 22-25; Transcript of the Hearing held on September 23, 2005, p. 34 lines 6-14; Transcript of the Hearing held on July 24, 2006, p. 132 lines 6-20.

and UHT are competitors in the fluid milk market. Their respective level of success is strongly influenced by their relative prices.[25] The price of fresh milk at all market levels is regulated. Pursuant to law, the maximum price set by the Administrator eliminated any adjustments to the income of the fresh milk processors resulting from price discounts previously considered, except as to the last price review issued by ORIL on April 19, 2007. On this date after being confronted with allowance of said adjustments to Indulac's price discounts were then re-established. The net effect is that the maximum price operates also as a minimum price for any margin calculations. The price of UHT is not regulated at any level. The price of UHT in Puerto Rico is customarily below that of fresh milk.[26]

8. The Association of Dairy Farmers groups the Puerto Rico dairy farmers and represents its interests. The dairy farmers have always opposed allowing the fresh milk processors to manufacture fluid milk in the form of UHT milk.[27] The dairy farmer sector has attempted several times to purchase the

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[25] See Transcript of the Hearing held on February 24, 2006, p. 61 lines 5-8; Transcript of the Hearing held on August 4, 2006, p. 46 line 20 - p. 47 line 3.

[26] See Transcript of the Hearing held on September 16, 2005, p. 89 line 6; Transcript of the Hearing held on September 23, 2005, p. 14 lines 8-9; Transcript of the Hearing held on November 1, 2005, p. 47 lines 11 -17; Transcript of the Hearing held on July 31, 2006, p. 11 line 19.

[27] See Transcript of the Hearing held on November 1, 2005, p. 69 line 24 - p. 70 line 19; Transcript of the Hearing held on June 20, 2006, p. 37 lines 2-14.

fresh milk processors.[28] The dairy farmers control the FFIL and control Indulac and want to consolidate in their hands the control of the whole industry.[29] The efforts to control the totality of the industry by eliminating the fresh milk processors, continued throughout the hearings.[30] Those efforts entail the participation of officials of the Government of Puerto Rico involved directly and indirectly in the milk industry and its price setting scheme.[31] The more desperate the financial condition of the fresh milk processors, the easier for the dairy farmers to acquire them or eliminate them.[32]

9. Plaintiffs are the only fresh milk processors currently operating in Puerto Rico. Suiza Dairy controls approximately 65.3% of the fresh milk market and Vaqueria Tres Monjitas ("VTM") controls

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[28] See Defendant's Exhibit C; Transcript of the Hearing held on October 24, 2005, p. 82 line 16 - p. 83 line 2; Transcript of the Hearing held on July 10, 2006, p. 8 line 13 - p.11 line 11; p. 17 line 8; Transcript of the Hearing held on August 1, 2006, p. 48 lines 5 - 7; Transcript of the Hearing held on May 9, 2006, p. 129 line 20 - p. 130 line 5.

[29] See Plaintiff's Exhibits 54 p. 2, 62 and 114; See also Transcript of the Hearing held on August 1, 2006, p. 26 line 2 - p. 27 line 20 and p. 29 line 8 - p. 30 line 22 and p. 36 line 11 - p. 37 line 7; Transcript of the Hearing held on May 9, 2006, p. 129 line 20 - p. 133 line 1.

[30] See Plaintiff's Exhibits 62 and 114; See also Transcript of the Hearing held on August 1, 2006, p. 26 line 2 - p. 27 line 20 and p. 29 line 8 - p. 30 line 22 and p. 36 line 11 - p. 37 line 7.

[31] See Transcript of the Hearing held on March 2, 2006, p. 2 line 22 - p. 3 line 16; Transcript of the Hearing held on June 30, 2006, p. 27 line 8 - p. 34 line 14.

[32] See Transcript of the Hearing held on September 26, 2005, p. 33 line 24 - p. 34 line 22.

34.7%.[33] Suiza Dairy formally requested a license to manufacture and market UHT milk and the same was denied by the Administrator.[34] Suiza presently sells an insignificant amount of UHT manufactured by Indulac under the brand Puerto Rico Dairy. That insignificant supply of UHT milk by Indulac to Suiza is deemed neither reliable nor consistent.[35]

10. Before the filing of this complaint, plaintiffs and the Administrator were still meeting to try to reach a solution to the milk industry controversy subject of this complaint.[36] To represent him in those conversations, the Administrator of ORIL appointed Mr. Samuel Torres, Esq. Mr. Torres is also an attorney for Indulac.[37] Mr. Torres is also the same person that on behalf of ORIL's Administrator stated in an ORIL hearing that the fresh milk processors had not been and never would be allowed to manufacture UHT milk.[38] Further, Fernando Tole-

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[33] See Defendant's Exhibit CC, Table 22. These numbers may have been slightly modified in favor of Tres Monjitas because of the routes resigned by Suiza assigned to Tres Monjitas. See Docket No. 446, Motion by Suiza advising of resignation of routes.

[34] See Plaintiff's Exhibits 9 and 10; Transcript of the Hearing held on November 1, 2005, p. 48 lines 11-15; p. 57 line 19 -p. 59 line 2; Transcript of the Hearing held on February 15, 2005, p. 140 line 16 - p.141 line 9.

[35] See Transcript of the Hearing held on February 15, 2005, p. 141 line 10- p. 142 line 6.

[36] See Plaintiff's Exhibits 2, 3, 4 and 5; see also Transcript of the Hearing held on February 28, 2006, p. 65 lines 2-11.

[37] See Transcript of the Hearing held on February 28, 2006, p. 80 line 20 - p. 82 line 22 and p. 87 lines 14-17. See also Plaintiff's Exhibit 2, 3, 4 and 5.

[38] See Plaintiff's Exhibits 78.

do, a Secretary of Agriculture, who is a life long dairy farmer, is the person who appointed the two public sector representatives of the Board of the FFIL.[39] Mr. Toledo is the same person that has been involved in the negotiations to buy the fresh milk processing plants, Suiza and VTM, co-plaintiffs in the instant case.[40]

11. The regulatory background of the underlying regulations is the following: Act 34 of June 11, 1957, P.R. Laws Ann. Tit. 5 §§ 1092-1118, as amended ("Act 34") provides ORIL broad authority to regulate the price of milk within the Commonwealth of Puerto Rico. Act 34 authorized the setting of minimum sales prices for raw milk and maximum sales prices for processed milk. In order to meet the legislative intent and mandates of Act 34, the Administrator of ORIL promulgated Regulation No. 1, with the approval of the Secretary of Agriculture.[41]

Article 16 of Act 34 (P.R. Ann. Tit. 5 § 1107 (a)-(e)) authorizes the Administrator to set the prices of milk at all levels. The law further establishes that "at least once a year" the Administrator is required to review the price of milk and make the necessary adjustment according to the increase and decrease of production costs as well as the operational expenses at all levels.

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[39] See Transcript of the Hearing held on February 28, 2005, p. 6 line 8 - p. 7 line 7.

[40] See Transcript of the Hearing held on February 15, 2005, p. 66 lines 6-17 and Transcript of the Hearing held on February 16, 2005, p. 243 line 21-p. 244 line 8.

[41] See Plaintiff's Exhibit 49.

From August 13th, 2004 and until recently (even after oral arguments), the Administrator of ORIL has been constantly and frequently shifting the targeted regulations by issuing a series of new regulations and administrative orders (not merely the yearly price regulations required by statute), changing the milk industry rules while the instant case was developing. During this period of time, ORIL amended the existing regulations and enacted new orders and resolutions changing the rules of the game of at least the following milk industry issues: (1) the price paid for the retained milk, (2) the price paid for the dairy farmers production within and over quotas, (3) the transportation reimbursement, (4) the reassignment of a determined number of dairy farmers from one processing plant to the other, and adjusting without holding a hearing a profitable and rentable fresh milk market shared by both processing plants, the school luncheon program and (5)the price paid by Indulac for surplus milk.

On August 12, 2005, defendants confirmed and admitted that the Regulation #1 had been vacated by the enactment of a new regulation, Regulation #10.[42] This representation led the Court to order plaintiff to amend the complaint to include the new regulation.[43] Subsequently, after expressing the court serious concerns about the validity of Regulation #10[44], defendants indicated that they were to

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[42] See Plaintiff's Exhibit 59 and Transcript of the Hearing held on August 12, 2005, p. 21, lines 22-25 and p. 22 lines 1-3.

[43] See Docket No. 206.

[44] See Transcript of the Hearing held on September 16th, 2005.

begin the rule making process anew since they agreed that Regulation #10 was invalid.[45] The Administrator of ORIL then began the process of enacting another regulation, Regulation #11, admitting that Regulation #10 was defective because the same had not been properly published.[46] As of this date, Regulation #11 has not been enacted.

Moreover, a year after the evidentiary hearings began on February 24, 2006 ORIL issued a Provisional Administrative Order[47] modifying the dairy farmer's compensation system and setting the price to be paid by Indulac at .32 cents.[48]

On November 30, 2006 ORIL issued a Provisional Administrative Order allowing Vaqueria Tres Monjitas to use surplus milk to substitute powdered milk used in the processing of ice cream, milk shakes and sour cream at the price of .25 cents per quart.[49]

On January 3, 2007 two new administrative orders were issued, one eliminating the .10 cents payment

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[45] See Transcript of the Hearing held on September 23, 2005, p. 58 line 18; See also 'Defendant's Informative Motion Regarding Regulation 10 and the Mootness Argument' filed on September 23, 2005 [Docket No. 210].

[46] See Transcript of the Hearing held on November 1, 2005, p. 14, lines 13-16.

[47] See Defendant's Exhibit AA.

[48] See detailed discussion on finding of fact # 36, 37, 38 of this Opinion and Order.

[49] See Exhibit 6 of Docket No. 448. Please refer to Exhibit 6 of Docket No. 464 for the certified translation of the same.

over quota of the dairy farmers' production[50] and the other one banning the leasing and sale of the dairy farmer's assigned quotas.

On January 31, 2007 ORIL enacted a Provisional Administrative Order authorizing Suiza to use surplus milk to substitute powder milk to manufacture the product Nesquik. Suiza was allowed to pay .25 cents per quart for the surplus milk used for this purpose.[51]

On February 7, 2007, without holding hearings of any kind, ORIL issued an Administrative Order transferring the production of certain dairy farmers from co-plaintiff Suiza to co-plaintiff Vaquerias Tres Monjitas. This change made an adjustment in the participation of the processing plants without a hearing in profitable fresh milk market, including the school luncheon program.[52]

On March 27, 2007 ORIL issued another Administrative Order that unilaterally and again without holding hearings, readjusted the participation of the processing plants in the school luncheon programs, decreasing 5.06% of Suiza's share and increasing Vaquerias Tres Monjitas' participation in the same equivalent amount. This order was subsequently amended on April 5, 2007 to establish that the same will be effective for the next school period,

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[50] See Exhibit 10 of Docket No. 446. Please refer to Exhibit 10 of Docket No. 469 for the certified translation of the same.

[51] See Exhibit 8 of Docket No. 448. Please refer to Exhibit 8 of Docket No. 464 for the certified translation of the same.

[52] See Exhibit 8 of Docket No. 450.

starting on August of 2007.[53] The court will not address any challenge as to the school luncheon program amongst the fresh milk processors since the court has held no hearings as to these matters.[54]

ORIL also issued another Administrative Order on April 5, 2007. As per Indulac's request, ORIL allowed Indulac to pay less than the .32 cents established by the Administrative Order of February 24, 2006 for the milk used to manufacture products others than UHT as cheese, powdered milk and evaporated milk.[55]

On April 19, 2007 ORIL issued a new Price Resolution[56] that left untouched the fresh processors price structure and failed to address properly any adjustments, nor a reasonable rate of return of the processing plants.[57] Finally, on June 13, 2007 ORIL issued an order reducing the farmers' compensation for raw milk.[58] None of these newly issued orders have diminished the merits of plaintiffs' claims.

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[53] See Exhibit 1 of Docket Nos. 456 and 465. Please refer to Exhibit 1 of Docket No. 470 for the certified translation of the same.

[54] Further there is no claim amongst the two fresh milk processors.

[55] See Exhibit 11 of Docket No.446. Please refer to Exhibit 11 of Docket No. 469 for the certified translation of the same.

[56] See Exhibit 12 of Docket No. 446. Please refer to Exhibit 12 of Docket No. 469 for the certified translation of the same.

[57] See detailed discussion on finding of fact #54 of this Opinion and Order.

[58] See Docket No. 474, Addendum 3.

12. The production of milk in Puerto Rico is cyclical,[59] meaning that less raw milk is produced during the hottest months of the year and more raw milk is produced during the coldest months.[60]

13. In 1952, Indulac was created with the purpose of handling the volume of raw milk produced in excess of the demands for raw milk in certain periods of the year.[61] Originally, and for many years, both the dairy farmers and the fresh milk processors had the same representation on Indulac's Board of Directors.[62]

14. For decades, fresh milk was the only kind of fluid milk that could be produced. At that time, milk produced in excess of the demands for fresh milk had to be turned into alternative products or destroyed.[63] For many years after its incorporation, Indulac was devoted to the production of cream, butter and cheese, products which have a lower rentability than fresh milk, but which do not compete with fresh milk.[64]

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[59] See Transcript of the Hearing held on October 18, 2006, p. 34 line 21 - p. 36 line 4.

[60] See Transcript of the Hearing held on March 1, 2006, p. 8 line 12 - p. 9 line 25; Transcript of the Hearing held on June 6, 2006, p. 19 line 16 - p. 21 line 6 and p. 30 lines 13 - 19.

[61] See Indulac's Certificate of Incorporation, Plaintiff's Exhibit 21.

[62] See Plaintiff's Exhibit 21.

[63] See Plaintiff's Exhibit 78, p. 32, lines 20-24; See also Transcript of the Hearing held on February 16, 2005, p. 416 line 13 - p. 417 line 10.

[64] See Plaintiff's Exhibit 21; See also Transcript of the Hearing held on February 16, 2005, p. 417 line 20 - p. 418 line 1.

15. Production of raw milk is much more expensive in Puerto Rico than anywhere else in the continental United States and more than in most other countries in the world.[65]

16. Initially, the agreement between the fresh milk processors and milk producers related to Indulac was that the same would operate to manage the volume of milk that in certain periods of the year exceeded the demand for fresh milk and turn said "surplus" into by-products that would not compete with fresh milk.[66]

17. For many years and as of this writing, pursuant to the decisions of the Administrator of ORIL and the regulations in place, the fresh milk processors have been required to collect all milk produced by the dairy farmers. The fresh milk processors would retain whatever milk they needed to satisfy the requirements of the fresh milk market and would then transport the rest of the raw milk ("surplus milk" according to the law) to Indulac for the manufacturing of milk by-products.[67] The cost of transportating Indulac's raw milk to Indulac's plants is reimbursed to the fresh milk processors through a formula approved by ORIL.[68] The *legal* definition of surplus milk is milk produced in excess of the market demands for fresh milk.[69] But as of this writing,

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[65] See Transcript of the Hearing held on June 6, 2006, p. 77 lines 6-9.

[66] See Transcript of the Hearing held on February 16, 2005, p. 416 line 16 - p. 418 line 8 and p. 445 lines 10-16. See also Plaintiff's Exhibit 21.

[67] See Plaintiff's Exhibit 49 § 6.

[68] See Plaintiff's Exhibits 64 and 65.

[69] Act 34 § 1096 (b) (4).

since fluid milk is processed as UHT by Indulac and warehoused without refrigeration, there is no surplus of fluid milk in Puerto Rico. If surplus is defined as milk processed in excess of fluid milk market demands, Puerto Rico does not produce enough fluid milk to satisfy itself on a yearly basis and thus no surplus exists.[70] Surplus milk constitutes a legal, not an economic, characterization.

18. The milk retained for production by the fresh milk processors had to be paid to the dairy farmers at the price set by the Administrator.[71] That price has always been one that is *well over* what is required by the dairy farmers to cover costs and make a reasonable profit.[72] This permitted the surplus milk purchased by Indulac to manufacture UHT to be paid by said entity at a price *much lower* than that required by the farmers to cover production costs.[73]

19. The farmers for years, and until the February 2006 order, received as compensation for their raw milk a weighted average resulting from the number of quarts of milk produced by fresh milk processors multiplied by the price set by the Administrator and the number of quarts declared surplus multiplied by the price of $0.10, which until the year 2006

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[70] See Defendant's Exhibit KK and Transcript of the Hearing held on March 2, 2006, p. 109 line 6 - p. 111 line 17. See also Transcript of the Hearing held on June 20, 2006, p 76 line 8 - p. 77 line 11.

[71] See Plaintiff's Exhibit 49.

[72] See Transcript of the Hearing held on May 8, 2006 p.39 lines 24-25 and p. 40 lines 1-2.

[73] See Transcript of the Hearing held on March 1, 2006 p. 28 lines 4-6.

remained the price set for surplus milk.[74] But de facto, Indulac has for years never paid less than $0.10 and in most cases did pay much more than $0.10 per quart for surplus milk.[75] Although Indulac before 2006, was not obligated to pay more than $0.10 per quart per surplus milk, it did so because that payment increased the amount of money received per quart by the dairy farmers.[76]

20. Although legally only the Administrator had the authority and duty to set the margin of the dairy farmers, the Administrator before 2006 never prohibited Indulac from increasing the same by increasing the amount paid for surplus milk. Thus Indulac, on its own, increased the farmers' margin.[77] Indulac has traditionally taken the position that its existence is justified precisely to increase the benefits to the farmers as high as possible, independently of ORIL's pricing regulations.[78]

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[74] See Plaintiff's Exhibits 124-126 and Defendant's Exhibit AA, Art. 8.

[75] See Defendant's Exhibit W.

[76] See Defendant's Exhibit W; See also Transcript of the Hearing held on October 24, 2005, p. 60-62; Transcript of the Hearing held on February 16, 2005, p. 438 line 13 - p. 439 line 9.

[77] See Defendant's Exhibit W; See also Transcript of the Hearing held on October 24, 2005, p. 60-62; Transcript of the Hearing held on February 16, 2005, p. 438 line 13 - p. 439 line 9.

[78] See Transcript of the Hearing held on October 25, 2005, p. 32 line 23 - p. 33 line 8; Transcript of the Hearing held on October 24, 2006, p. 64; Transcript of the Hearing held on February 16, 2005, p. 423; Transcript of the Hearing held on November 3, 2005, p. 171-172; Transcript of the Hearing held on June 5, 2006, p. 74 line 22 - p. 75 line 2.

21. In other words, Indulac payments were generally as follows. Indulac paid $0.10 cents per quart of raw milk. If that was enough to reach or exceed the farmers' weighted average compensation as set by Indulac, Indulac did not pay more. If with that contribution the farmer's weighted average did not reach Indulac's predetermined desired level, Indulac would put in the additional monies until that level was reached. In both cases, Indulac would contribute further amounts to finance certain FFIL's programs and to service through the FFIL loans taken for Indulac's benefit.[79]

22. Even by paying the dairy farmer an amount greater than the regulated amount of $0.10 per quart for surplus,[80] the total cost of milk to Indulac was well below the production cost of the dairy farmers.[81] This fact is economically correct even if Indulac's contribution to the FFIL programs and the debt service of Indulac's loans are considered as cost of milk, as Indulac did.[82]

23. Indulac pays well below production costs for its raw material as the processors of fresh milk are required to pay much more than production cost and reasonable profit for each quart of milk they

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[79] See Transcript of the Hearing held on March 2, 2006, p. 132 line 14 - p. 133 line 20; Transcript of the Hearing held on May 9, 2006, p. 141 line 11 - p. 148 line 25; p. 143 lines 15-24; Transcript of the Hearing held on May 10, 2006, p. 10-11; Transcript of the Hearing held on June 30, 2006, p. 34 line 17 - p. 39 line 2.

[80] See Defendant's Exhibit W.

[81] See Transcript of the Hearing held on February 24, 2006, p. 56 lines 1 - 6.

[82] See Plaintiff's Exhibit 52 p. 3.

retain for fresh milk. Through said imposed method, the farmer's average is not affected by Indulac's below cost price. The final result is unquestionably that fresh milk processors in effect subsidize with their very high cost per quart Indulac's very low cost.

24. During the mid-eighties, a change was introduced to the farmer's compensation system. Up to that moment, the weighted average received by the farmer for the totality of his production within quota varied depending on the processor to which the farmer sold his milk. This was the case as different processors had different levels of retained vs. surplus milk. Dairy farmers selling their milk to processors with a high percentage of retained milk received a higher weighted average than those dairy farmers selling milk to fresh milk processors with a higher percentage of surplus. In the year 1985, when Mr. Luis Fullana was head of ORIL, a regulatory change was introduced pursuant to which the weighted average for all dairy farmers on the Island was to be calculated on the basis of island-wide proportion of retained milk vs. surplus regardless of the situation of each individual processor. From that time on, every dairy farmer in Puerto Rico has received the same compensation per quart of raw milk for every single quart produced within quota, regardless of the processor to which that farmer is attached.[83]

25. By the year 1998, Indulac was aggressively marketing UHT and devoting as much surplus milk as

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[83] See Transcript of the Hearing held on October 18, 2005, p. 19 line 6 - p. 23 line 7.

possible to its production.[84] Indulac's main product today is unquestionably the manufacture of UHT.[85] Indulac's pricing strategy for its UHT is to meet or beat the low price at which that product is introduced into Puerto Rico by foreign producers.[86] For years that price has been consistently and substantially lower than the price of fresh milk.[87]

26. The price at which UHT milk is sold in Puerto Rico is basically set by imported UHT milk since the Continental United States enjoys a lower price for raw milk than the cost in Puerto Rico.[88] That milk comes into Puerto Rico from mainland United States and is sold to the consumer. However, contrary to what occurs in mainland United States, where UHT is normally sold at a price much higher than fresh milk, the opposite is true in Puerto Rico.[89] UHT consumer prices in Puerto Rico have been consistently lower than the regulated price of fresh milk.[90] In order to compete with UHT im-

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[84] See Transcript of the Hearing held on March 1, 2006, p. 29.

[85] See Transcript of the Hearing held on March 1, 2006, p. 29.

[86] Transcript of the Hearing held on August 22, 2005, p. 86 lines 11-14; Transcript of the Hearing held on July 24, 2006, p. 129 lines 21-25; Transcript of the Hearing held on July 24, 2006, p. 131 lines 3-5; p. 158 lines 13-16; Transcript of the Hearing held on June 19, 2006, p. 68 lines 6-8; p. 71 lines 11-25; p. 76 lines 14-17; p. 78 lines 10-25.

[87] See Transcript of the Hearing held on September 16, 2005 p. 38 lines 18-22 see also Transcript of the Hearing held on February 15, 2005, p. 42 lines 8-16.

[88] See Transcript of the Hearing held on August 4, 2006, p. 36 lines 1-9; Transcript of the Hearing held on June 19, 2006, p. 70 lines 4-8.

[89] See Transcript of the Hearing held on August 22, 2005 p. 80 lines 7-9.

[90] See Plaintiff's Exhibits 34, 46 and 71 at p.3.

ports, Indulac has to match or beat that low price. In doing so, Indulac competes against both UHT imports and plaintiffs' fresh milk.[91] Due to the high cost of producing milk in Puerto Rico, Indulac can only so act by paying for raw milk a price well below actual production cost of the dairy farmers.[92] Without its regulatory subsidized price by the fresh milk processors for raw milk, Indulac would not be able to compete with the UHT importers. Indulac consequeantly takes over a substantial portion of the Puerto Rico fluid milk market and enjoys a competitive edge over the importers.[93] Undisputably, the purpose and effect of Indulac's subsidized price for raw milk is to deprive importers of UHT of their natural low price advantage in order to preserve the local milk market for the local milk producers. The admissions of defendants themselves so demonstrate. The Administrator of ORIL said on the stand:

> "If right now, instead of .32 cents we were to raise the price of surplus milk to .53, .55 cents, and we lower the price

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[91] See Transcript of the Hearing held on October 24, 2005, p. 151-152; Transcript of the Hearing held on February 16, 2005, p. 422 line 19-21; Transcript of the Hearing held on July 7, 2005, p. 63 line 6-14; Transcript of the Hearing held on June 19, 2006, p. 69 line 20 - p. 71 line 18; Transcript of the Hearing held on August 1, 2006, p. 45-46.

[92] See Transcript of the Hearing held on June 19, 2006, p. 70 lines 1-23, p. 76 lines 1-25; Transcript of the Hearing held on August 4, 2005, p. 30; Transcript of the Hearing held May 9, 2006, p. 128 lines 13-16.

[93] See Transcript of the Hearing held on May 9, 2006, p. 128 lines 13 - 16. See also Transcript of the Hearing held on June 19, 2006, p. 70 lines 1-23 and p. 76 lines 1-25.

> of fresh milk to .53 or .55 cents in order for Indulac to be able to have a profit and continue in operation, we are going to have to raise the price of UHT milk to 1.30 or 1.50 per liter or quart. And if we are going to do that today without these two [protectionist] bills of law, the imported UHT milk is going to take over the entire [UHT] market and it will make Indulac go bankrupt. . . "[94]

At another point Mr. Pedro answered as follows a question in cross examination:

> **Q.** (Mr. Escalera) Mr. Pedro, the fact is that you know that without the subsidy we have just discussed, Indulac would not be capable to compete with imported UHT. Right?
>
> **A.** Yes.[95]
>
> The Chief Executive Officer of Indulac Mr. Benitez responded as follows in cross examination:
>
> **Q.** (Mr. Escalera) So, Indulac has to buy its raw milk well below production cost in order to be able to compete with imported UHT, right?
>
> **A.** That's correct.[96]

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[94] See Transcript of the Hearing held on February 27, 2006, p. 34 line 19 - p. 35 line 3.

[95] See Transcript of the Hearing held on May 9, 2006, p. 128.

[96] See Transcript of the Hearing held on June 19, 2006, p. 76 lines 14-17.

Both the expert for the Farmers Association, Mr. Feliciano, and the expert for Indulac, Mr. Schaffer, testified in the same sense.[97]

27. This regulatory created scheme has provoked a consistent growth in UHT and a consistent decline in the sales of fresh milk.[98] From 1998 through 2004 fresh milk sales declined from 318.50 million quarts to 275.27 million quarts. In the same periods, sales of UHT milk increased from 38.40 million quarts to 69.93 million quarts. Fresh milk sales have decreased at 2.4% per year while UHT milk has increased 10.5% per year since 1998. Evidently, since plaintiffs are not allowed to process UHT, they retain only the raw milk necessary to satisfy the declining demand for fresh milk. When the demand for fresh milk falls, less fresh milk is retained and less milk at the higher price went originally into the weighted average calculation (and now into the money pool) from which the farmer is paid for its raw milk. Stated differently, a decrease in the demand of fresh milk (made from retained milk) and an increase in the demand for UHT (made from surplus) affected negatively the farmer's average and now the possibility of paying the farmer at the established level.[99] Before the February 2006 order, this problem was dealt with by voluntary increases

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[97] See Transcript of the Hearng held on July 24, 2006 p. 129 and Transcript of August 4, 2006 p. 6.

[98] See Plaintiff's Exhibits 28-30; Transcript of the Hearing held on August 22, 2005, p. 39 line 21 - p. 40 line 2; Transcript of the Hearing held on September 20, 2005, p. 67 lines 4-11; Transcript of the Hearing held on August 24, 2005, p. 43-44.

[99] See Transcript of the Hearing held on May 8, 2006, p. 10 lines 10-17, 22.

in the amounts contributed by Indulac for farmers' compensation and mandatory increases required by ORIL in the price paid by fresh milk processors for retained milk.[100] Indulac's increased contributions to the average came out of its high profits (multimillion dollars) in the UHT business achieved by subsidized price of raw milk.[101]

28. By the year 2002, the Board of Indulac began to guarantee a minimum payment to the farmer.[102] That guarantee was set by Indulac and not by ORIL. This meant that in every biweekly liquidation in which the weighted average would go below the guaranteed minimum payment, Indulac would put whatever amount was necessary over the $0.10 it was required to pay for surplus milk, in order to take the average for the totality of production within quota to the now guaranteed level.[103] This level was the amount necessary to cover the farmer's cost and a profit as determined by Indulac. Through this method the farmer had the certainty that what Indulac would pay for the raw milk over and above the required $0.10 would in turn translate into a certain fixed minimum guaranteed compensation per quart for each and every farmer. In-

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[100] See Defendant's Exhibit W and Plaintiff's Exhibit 12; Transcript of the Hearing held on October 24, 2005, p. 74-77.

[101] See Plaintiff's Exhibit 36, 102, 102A, 108 and 109; see Transcript of the Hearing held on February 27, 2006, p. 34-p. 35.

[102] See Transcript of the Hearing held on May 8, 2006, p. 22 line 23 - p. 24 line 3.

[103] See Transcript of the Hearing held on October 24, 2005, p. 60, 64; Transcript of the Hearing held May 8, 2006, p. 21; Transcript of the Hearing held June 6, 2006, p. 45 lines 8-16.

dulac increased the farmer's guarantee several times since 2002.[104] The Administrator did not intervene with this guarantee nor did he at any time impede the farmer's margin as set by Indulac.[105] There has never been statutory or regulatory authority for these acts by Indulac.

29. After contributing the money for the farmer's guarantee, Indulac proceeded to contribute to the FFIL programs and to pay the debt service of its loans.[106]

30. The UHT business has been extremely productive to Indulac to the point that Indulac decided to devote all its milk to UHT while buying milk in the United States to manufacture Puerto Rican cheese.[107] The key to Indulac's profitability is precisely Indulac's purchase of raw milk at below cost of production prices. That low price as stated before is possible only because of the fresh milk processors excessively high price for the same milk.[108]

31. In December of that same year, 2002, the law regulating the milk industry was amended to give the

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[104] See Transcript of the Hearing held on May 8, 2006, p. 22 lines 23 - p. 23 line 18.

[105] See Transcript of the Hearing held on May 8, 2006, p. 21 lines 5-19 and p. 25 line 19-p. 27 line 4.

[106] See Transcript of the Hearing held on June 16, 2006, p. 16 lines 8-18.

[107] See Transcript of the Hearing held on March 2, 2006 p. 21 lines 9 - 19.

[108] See Transcript of the Hearing held on February 16, 2005, p. 431 lines 8-13.

farmers full and "*de jure*" control of the FFIL.[109] At the same time, the by-laws and certificate of incorporation of Indulac (which for years had provided for equal representation of farmers and fresh milk processors on Indulac's board) were amended to exclude the fresh milk processors from the Board of Indulac against their will.[110] These amendments also included the elimination of the prohibition to Indulac to enter into the fresh milk business and an express authorization for Indulac to fully compete in all areas with the fresh milk processors and other participants of the milk and related industries.[111] All legal limitations Indulac previously had to operate as a full and modern corporate competitor as to fresh milk were then eliminated; however, the fresh milk processor (Suiza) continued with a denial of a permit to manufacture UHT.[112]

32. The UHT phenomena turned Indulac into a major player in the fluid milk market in Puerto Rico. De-

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[109] P.R. Laws Ann.Tit. 5 § 1099 as amended by Act No. 278 of December 19, 2002.

[110] See Exhibits 7, 8, 22, Article 6(a), (b), 57, Article 6, 66 p. 7, 67, 68, and 69; Transcript of the Hearing held on November 1, 2005, p. 45 line 23 - p. 46 line 24; Transcript to Hearing held on February 28, 2006, p. 26, 29; p. 31 line 25 - p. 45 line 2; p. 55-60; Transcript to Hearing held on October 24, 2005, p. 68 line 1 - p. 69 line 7; Transcript to Hearing held on February 15, 2005, p. 21 line 7 - p. 22 line 14.

[111] See Plaintiff's Exhibit 22; Transcript of the Hearing held on July 7, 2005, p. 119 lines 22-24; Transcript of the Hearing held on May 9, 2006, p. 128 line 19 - p. 129 line 19.

[112] Of course, a license to produce UHT for the fresh milk processors is meaningless unless they are given the same low price for said milk that Indulac receives.

spite this obvious fact, Indulac continued to operate within a regulated market but in an unregulated fashion.[113] Indulac continued to decide without the Administrator's participation how much to pay the dairy farmers for the surplus milk.[114] Indulac did so despite the fixed price set for this milk by the regulation in place. Furthermore, although the operation of the fresh milk processors was subject to analysis and review every year in order to set prices for all levels of fresh milk, Indulac was never subject to a similar examination or audit.[115] By deciding how much extra money to pay for its raw milk, Indulac was deciding de facto the level of compensation of the dairy farmer that was by statute to be set by the Administrator.[116]

33. Since the Board of Indulac is composed of dairy farmers, the decision of those farmers to set the margin of the producers was in fact a decision to set their own personal margins.[117]

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[113] See Transcript of the Hearing held on October 24, 2005, p. 65 lines 13-17; see also Transcript of the Hearing held on June 16, 2006, p. 47.

[114] See Transcript of the Hearing held on May 8, 2006, p.1 21 lines 5-19.

[115] See Transcript of the Hearing held on October 24, 2005, p. 51-55; Transcript of the Hearing held on June 16, 2006, p. 47 lines 16-18; Transcript of the Hearing held on June 30, 2006, p. 41 lines 8-10.

[116] See Transcript of the Hearing held on July 26, 2006, p. 124 line 11 - p. 125 line 3; Transcript of the Hearing held on March 2, 2006, p. 131 line 11 - p. 132 line 12; Transcript of the Hearing held on June 6, 2006, p. 46 lines 15-18; p 49 line 16 - p. 50 line 14; p. 52 lines 5-7.

[117] See Transcript of the Hearing held on July 26, 2006, p. 124 line 11 - p. 125 line 3, p. 127 lines 10-21.

34. Indulac was not only entitled to decide how much to pay for it's raw milk, but it was free to decide how much to charge for it's processed UHT.[118] In other words, this fluid milk competitor within the regulated milk market of Puerto Rico could decide freely its own margin and profit, and further was able to determine the profit of the dairy farmers. Of the three major players of the Puerto Rican milk industry (dairy farmers, Indulac and the fresh milk processors) only the latter was not controlled by the farmers and only the latter had its margin actually regulated by the Administrator.[119]

35. On account of a dispute regarding which price regulation issued by ORIL was actually in place, well into in the middle of these injunction hearings, the Administrator issued on February 2006 a provisional order that modified the dairy farmers' compensation system. Without holding hearings of any kind, and without ever having conducted an examination of the operations of Indulac[120], the Administrator set the price to be paid by Indulac for raw milk at $0.32.[121] This payment was not only coincidentally the price at which Indulac had unilaterally decided shortly before to pay for the milk,[122] but al-

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[118] See Transcript of the Hearing held on July 26, 2006, p. 124 line 11 - p. 125 line 3 and p. 127 lines 10-21; see also Transcript of the Hearing held on May 8, 2006 p. 10 lines 4-17.

[119] See Transcript of the Hearing held on October 24, 2005, p. 51-55.

[120] See Transcript of the Hearing held on October 24, 2005, p. 51-55; Transcript of the Hearing held on June 16, 2006, p. 47 lines 16-18.

[121] See Defendant's Exhibit AA.

[122] See Plaintiff's Exhibits 102, 110, and Defendant's Exhibit CCC; See also Transcript of the Hearing held on March 2, 2006, p. 35 line

so the price which Indulac had represented in writing to the Administrator that it could pay for the milk and still make a reasonable profit.[123] The Administrator took Indulac's word at face value. The fresh fluid producers were never consulted. Indulac's profit projections presented to the Administrator contemplated substantial income from the juice business, an unregulated activity which is the main source of income to the fresh milk processors. Indulac was to continue to pay below cost for raw milk and use that advantage to further compete with the fresh milk processors in their other profitable lines of unregulated business. At that time, Indulac began to compete with the fresh milk processors in the juice business.[124]

36. The February 2006 order capped Indulac's risk by setting the price Indulac was to pay for its raw milk at the level Indulac requested, that is $0.32.[125] Indulac no longer was at risk of having to invest additional monies to raise the weighted average to the level of the guarantee. Indulac was thus insulated from the risk of financial exposure on account of a

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13 - p. 36 line 24;Transcript of the Hearing held on May 12, 2006, p. 41 line 19 - p. 42 line 18; p. 45 lines 14-24.

[123] See Transcript of the Hearing held on February 27, 2006, p. 23 lines 2-6; Transcript of the Hearing held on May 12, 2006, p. 42 line 4-6.

[124] See Transcript of the Hearing held on June 19, 2006, p. 32 line 18 - p. 33 line 24; Transcript of the Hearing held on May 12, 2006, p. 41 lines 1-6; Transcript of the Hearing held on May 11, 2006, p. 27 line 24 - p. 28 line 9.

[125] See Defendant's Exhibit AA, Art. 8; Transcript of the Hearing held on June 12, 2006, p. 20 line 16 - p. 21 line 16; Transcript of the Hearing held on May 8, 2006, p. 50 lines 13 - 15.

rise in the amount of raw milk devoted to UHT ("surplus") vs. the amount devoted to fresh milk ("retained milk"). ORIL relieved Indulac of the economic burden of having to increase payment for milk (to stabilize the farmers' income) as the demand for fresh milk continued to decrease at least in part because of Indulac's own efforts to market UHT. Additionally, Indulac was relieved of the burden of paying for the Fund's loans taken for Indulac's benefit and programs which would now come out of the money paid by Indulac *and the processors* of fresh milk as opposed to coming exclusively from Indulac's profits.[126] Despite these benefits to Indulac the Administrator's order did nothing to alleviate the problems created by Indulac's subsidized UHT or plaintiffs excessive cost of raw milk.

37. Under this provisional order, the payment fund has been in deficit practically from day one.[127] From the monies contributed by the fresh milk processors and Indulac the farmers are paid first, the loans and programs are second in line, and any remaining amount returns to the fresh milk processors. But, the system is running a multi-million dollar deficit simply to satisfy loans and programs and, as we will see, even to pay the farmers.[128] Evidently, if no money is left to pay for loans, programs and the

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[126] See Transcript of the Hearing held on March 2, 2006, p. 132 line 14 - p. 133 line 20; Transcript of the Hearing held on May 10, 2006, p. 10 line 6 - p.11 line 9; Transcript of the Hearing held on June 30, 2006, p. 34 line 17 - p. 39 line 2.

[127] See Plaintiff's Exhibits 84-93, and 95.

[128] See Plaintiff's Exhibits 124-126.

farmers much less is there to be money available to alleviate the critical situation of the processing plants. A loan of over $2 million by Indulac to the Fund reduced the deficit to $1 million in February of 2007. In only three months the deficit of the Fund went from $1 million to almost $4 million.[129] The deficit in the last biweekly period of the month of May 2007 grew by almost $1 million in just two weeks[130]. The deficit as of June 13, 2007 was already $6,110,940.34. The situation has reached to the point that the money available is not even enough to pay the farmers, the first priority of the payment fund.[131] This fault occurred even though now the over-quota milk is not paid for at all. Over quota milk is milk produced by a farmer in excess of that farmer's production quota. That is, of course, different from "surplus" which is the island-wide production of milk that in a particular period exceeds the market demand for fresh milk. This milk was for decades paid at 10 cents per quart. These situations provoked a new order dated April 19, 2007.[132] In this order the compensation of the farmer is further reduced. Although the Administrator concluded that for the year 2005 in which the last price increase became effective, the dairy farmers suffered a reduction in margin from 8.84 cents per quart to 5.28 cents per quart, their milk is now

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[129] See Exhibit 1 of Docket No. 463.

[130] See Exhibit 1 of Docket No. 463 and addendum of Docket No. 474.

[131] See Exhibits 1 to 8 of Docket No. 446, Exhibit 1 of Docket No. 463 and Addendums 1 and 2 of Docket No. 474.

[132] See Exhibit 12 of Docket No. 446.

going to be paid as follows: 5% of the milk produced within quota will not be paid at all, 95% of the quota will be paid according to the following scale: 70% at $0.55 per quart, 20% at $0.50 per quart and 10% at $0.30 cents per quart. It was the Dairy Farmers Association itself that suggested these reductions on June 6, 2007. Despite the fact that this is an order of price setting, it took the Administrator less than a week to find that suggestion acceptable and to adopt it in its order. The Fund now is incapable of providing monies neither for the payment of the programs nor for the servicing of Indulac's loans, or even to keep the farmers' compensation at the 2005 level.

38. This system is about to cause the industry to collapse. In no market of the United States does UHT play the large role it plays in Puerto Rico.[133] The evidence shows that fresh milk is in continuous rapid pace decline. The system is also placing the farmer's compensation at risk, as the milk transportation infrastructure is exclusively provided by fresh milk processors and consequently[134] a threat to them is a threat to the industry. Lately the amount of surplus milk has increased beyond Indulac's handling and marketing capabilities. As a result,

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[133] See Transcript of the Hearing held on July 11, 2006, p. 87 lines 9-24; p. 105 lines 5-10; p. 134 lines 13-20; Transcript of the Hearing held on August 4, 2006, p. 21 lines 13-25.

[134] See Transcript of the Hearing held on July 11, 2006, p. 87 lines 9-24; p. 105 lines 5-10; p. 134 lines 13-20; Transcript of the Hearing held on August 4, 2006, p. 21 lines 13-25.

substantial amounts of raw milk are being destroyed.[135]

39. The February 2006 order establishes the farmer's compensation (recovery of costs and profit) at $0.55 per quart of raw milk produced within quota. This amount is coincidentally exactly the same guarantee that Indulac had in effect for the farmers before the provisional order.[136] The February 2006 order set the fresh milk processors' price at 66.125 cents for the same milk for which Indulac merely paid $0.32 per quart.[137] But now, not only the farmers' compensation has been reduced as indicated but the Administrator has also reduced Indulac's cost of milk. On April 5, 2007 the Administrator issued another order[138] establishing new prices for Indulac's raw milk according to the use to which said milk was to be destined. The new order reduced the price substantially for important portions of Indulac's raw milk. Indulac's new raw milk price structure is as follows: UHT milk $0.32, evaporated milk and powdered milk $0.12, cheese $0.20. Again, ORIL established those prices exactly as requested by Indulac. The Administrator made it clear that this new advantageous price structure would be available *exclusively* to Indulac. The liquidations for the period ended May 6, 2007[139] de-

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[135] See Plaintiff's Exhibit 111, p.2; See also Transcript of the Hearing held on June 20, 2006, p. 51 lines 5-18.

[136] See Transcript of the Hearing held on June 16, 2006, p. 53 line 25 - p. 54 lines 1- 3.

[137] See Defendant's Exhibit AA.

[138] See Addendum 11 of Docket No. 446.

[139] See Exhibit 8 of Docket 446.

monstrates via a proffer by Suiza that the Administrator has basically reduced Indulac's raw milk price from $0.32 to approximately $0.265. This is a reduction in Indulac's cost of milk and contribution to the farmers' payment fund of 17.3%.

40. ORIL is required by law to review every year the situation of the milk industry and adjust the prices of fresh milk accordingly.[140] At least one year ORIL conducted no price review simply because Suiza had changed owners.[141] On another occasion ORIL did not issue a resolution regarding the price of milk because lack of auditing staff to perform the task.[142] ORIL has no mechanism in place for automatic price adjustments on the basis of changes in costs between yearly price revisions. Since all price reviews are prospective and normally the order is effective months after the end of the cost period used for evaluation, the fresh milk processors never recover the losses on account of increased expenses and decreased volumes in the interval between reviews. Additionally ORIL has no regulatory standards whatsoever to judge fairly the profit margin of the fresh milk processors.[143] The rules of cost analysis (if they exist) are not notified in advance and they in fact vary from year to year. The

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[140] See Act 34 § 1107(c).

[141] See Transcript of the Hearing held on November 3, 2005, p. 83 lines 11-21. See also Transcript of the Hearing held on February 15, 2005, p. 190 line 4 - p. 191 line 13.

[142] See Transcript of the Hearing held on February 24, 2006, p. 76 lines 10-19.

[143] See Transcript of the Hearing held on September 23, 2005 p. 9 lines 10 - 22.

net result is an artificial reduction in the amount of expenses allowed to the plants[144] and an artificial upwards increase in their income.[145] The 2007 price order achieves this increase by considering as fresh milk income money derived from unregulated business activities.[146] This manipulation of plaintiffs' real financial picture is the consistent result, year after year, albeit on account of ever changing regulatory criteria.

41. The last price change for fresh milk processors was effective in May 2005. For the same, ORIL used cost numbers of the natural year 2003[147] despite the fact that ORIL had available the cost numbers for the first half of the year 2004.[148] ORIL concluded despite being well aware that certain very important cost items such as fuel, electricity and resin had sky-rocketed for the year 2004.[149]

42. This decision by ORIL seriously underestimated the costs of the plants for the period in which the

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[144] See Transcript of the Hearing held on September 20, 2005, p. 21 line 19 - p. 22 line 15.

[145] See Transcript of the Hearing held on September 20, 2005, p. 26 lines 3- 20 and p. 57 lines 4 - 13.

[146] See Exhibit 12 of Docket No. 446.

[147] See Transcript of the Hearing held on May 8, 2006, p. 71 line 18 - p. 72 line 25; Transcript of the Hearing held on September 20, 2005, p. 16 line 24 - p. 17 line 7.

[148] See Transcript of the Hearing held on May 8, 2006, p. 48 line 23 - p. 49 line 25.

[149] See Transcript of the Hearing held on September 23, 2005, p. 15 lines 19-23; Transcript of the Hearing held on September 20, 2005, p. 62 lines 1-10; Transcript of the Hearing held on May 9, 2006, p. 65 lines 1-20.

new prices would be in effect. Even as of the date of this order, the plants continue to operate under a price structure based on the year 2003 cost numbers and volumes,[150] despite a proffered increase by Suiza to the plants of 61.60% in the cost of gasoline, 41.22% in the cost of electricity and 49.59% increase and in the cost of resin to Suiza together with a continuously sharp decrease of sales volumes.[151]

43. During the review process for the price increase effective May 2005, ORIL for the first time, adjusted upwards the income from fresh milk sales by plaintiff.[152] Instead of determining the real amount of money collected by plaintiff on account of those sales, the Administrator simply established the plants' income by multiplying the amount of milk sold by the regulated price.[153] By doing this, ORIL for the first time in unannounced fashion eliminated the adjustments made to sales figures by the plants on account of milk returns as similar loss factors that had been previously accepted. ORIL had no regulatory parameters on this issue, nor did it provide any evidence rationale to support this decision. Nevertheless, although the 2007 price order left untouched the price structure of plaintiffs,

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[150] See Defendant's Exhibit K; Transcript of the Hearing held on August 4, 2006, p. 103 line 25 - p. 107 line 11.

[151] See Exhibits 13 and 14 of Docket No. 446. See Exhibit 13 of Docket No. 469 for the certified translation of the same.

[152] See Plaintiff's Exhibit 81. See also Transcript of the Hearing held on May 8, 2006, p. 75 line 17 - p. 76 line 15.

[153] See Transcript of the Hearing held on May 8, 2006, p. 74, lines 10-25.

those adjustments and disallowances were not made.[154]

44. Similarly, for the order effective May 2005, the Administrator was disallowing the adjustments to income resulting from discounts to agents and other promotions. The position of the Administrator was that these discounts were illegal.[155] Nonetheless, ORIL had previous to 2005 admitted at least certain amounts of adjustments on account of these promotions and discounts without regulatory parameters for the same.[156] Competitor Indulac also in the milk business regularly provided discounts not opposed by the regulator as an essential part of its marketing strategy.[157] The Administrator has never intervened with Indulac in this regard. The same law that the Administrator interpreted to apply to the fresh milk processors and was used by the Administrator for these disallowances, applied equally to Indulac.[158] (The Administrator also sits on the Board of Indulac.) Lastly, Indulac incurs in the same agents' cost as the fresh milk processors without ORIL's intervention.[159] As a matter of fact,

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[154] See Exhibit 12 of Docket No. 446. See Exhibit 12 of Docket No. 469 for the certified translation of the same.

[155] See Transcript of the Hearing held on May 8, 2006, p. 129 lines 14-23.

[156] See Transcript of the Hearing held on November 3, 2005, p. 54 line 1 - p. 57 line 15.

[157] See Transcript of the Hearing held on May 8, 2006, p. 140 lines 10 - 15 and p. 95 lines 7 - 21.

[158] See Transcript of the Hearing held on May 8, 2006, p. 139 line 21 - p. 140 line 6.

[159] See Defendant's Exhibits P and Q; Transcript of the Hearing held on May 9, 2006, p. 4 line 7- p. 5 line 15.

in a letter to the Administrator following up on Indulac's September 8, 2006 letter requesting a price reduction to the Administrator, Indulac openly states to ORIL that offers and discounts of UHT would last three months and estimates that it would have a total of $1,840,000.00 of offers and discounts. In the following paragraphs Indulac admits that during the year 2006 it has granted substantial offers and discounts due to inventory obsolescence.[160]

45. Shrinkage is the loss of milk production inherent to any milk manufacturing process. The price order effective in the year 2005 made a substantial reduction on the shrinkage factor claimed by the plants. ORIL simply explained this adjustment by stating that the shrinkage factor it was applying has been historically used by ORIL. The evidence demonstrates this to be totally untrue. The 2005 shrinkage factor of $0.0075 had never been applied before.[161] The Administrator has never performed a study to determine the reasonable shrinkage factor that should be applicable in Puerto Rico, nor has he approved any regulatory standard on the same.[162] The shrinkage factor claimed by plaintiffs compares very favorably with the average shrinkage factors accepted in geographic parallel regions less affected by heat in Continental United States, al-

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[160] See Exhibit 2 to Indulac's motion Docket No. 448. Please refer to Exhibit 2 of Docket No. 464 for a certified translation of the same.

[161] See Plaintiff's Exhibit 81; Transcription of Hearing held on May 8, 2006, p. 91 line 13 - p. 93 line 3.

[162] See Transcript of the Hearing held on May 8, 2006, p. 106 line 13 - p. 107 line 6; Transcript of the Hearing held on September 20, 2005, p. 36 lines 2-10.

though temperature constitutes undisputably a key critical factor increasing shrinkage.[163] In the 2007 price order the shrinkage factor "historically applied" changed to $0.0088.[164]

46. For the price order effective May 2005, the Administrator examined the cost of plastic and professional fees of both plants.[165] In each case, he used for both the lowest of the figures presented by either of the two plants. ORIL had no evidence that Suiza was paying its plastic caps and bottles above market price.[166] ORIL had no evidence of overpayment by Vaqueria Tres Monjitas for professional fees.[167]

47. ORIL disallowed the experts' fees paid by the fresh milk processors for work related to the rate proceedings and regulation by ORIL.[168] It did so with-

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[163] See Transcript of the Hearing held on September 23, 2005, p. 20 lines 18-22; Transcript of the Hearing held on May 8, 2006, p. 109 line 23 - p. 110 line 24.

[164] See Exhibit 12 of Docket No. 446.

[165] See Transcript of the Hearing held on September 20, 2005, p. 39 line 20 p. 44 line 2; p. 45 line 24 p. 47 line 10; Transcript of the Hearing held on September 23, 2005, p. 15; Transcript of the Hearing held on November 3, 2005, p. 25 line 19 - p. 27 line 9; p. 49 line 2 p. 51 line 24; Transcript of the Hearing held on May 9, 2006, p. 33 line 13 p. 38 line 18; p. 38 line 19 p. 42 line 17.

[166] See Transcript of the Hearing held on September 23, 2005, p. 15; Transcript of the Hearing held on May 9, 2006, p. 39 lines 15-24.

[167] See Transcript of the Hearing held on September 23, 2005, p. 24 line 4 p. 27 line 3; Transcript of the Hearing held on May 9, 2006, p. 33 line 14 p. 34 line 7.

[168] See Transcript of the Hearing held on September 20, 2005, p. 53 lines 1-9; Transcript of the Hearing held on May 9, 2006, p. 110 lines 17-25.

out any evidence that these expenses were excessive.[169]

48. To determine the price at which milk should be sold to allow the fresh milk processors to obtain a reasonable profit by way of a reasonable return on capital, ORIL determines the capital base, divides it by the number of quarts sold and obtains the capital per quart of milk sold.[170] But in using said method ORIL uses the amount of milk sold during the base year of examination, which for the order effective on May 2005 was calendar year 2003.[171] ORIL did this although by the time it issued its April 2005 order, the year 2004 had transpired demonstrating that the amount of fresh milk sold during that year had substantially decreased compared to the year 2003. This decreasing trend has been consistent for the last few years.[172] Despite the decreasing trend, ORIL issued its year 2005 order with year 2003 volumes that it knew were fictitious since the Administrator had then available figures prepared by his own office.

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[169] Id.

[170] See Transcript of the Hearing held on May 9, 2006, p. 44 line 12 - p. 49 line 17.

[171] See Transcript of the Hearing held on May 8, 2006, p. 71 line 18 - p. 72 line 25; Transcript of the Hearing held on May 9, 2006, p. 50 lines 3-18; p. 45 line 16 p. 46 line 8.

[172] See Plaintiff's Exhibits 28 and 29; Defendant's Exhibit KK; Transcript of the Hearing held on February 16, 2005, p. 423-425; Transcript of the Hearing held on August 22, 2005, p. 29-30; Transcript of the Hearing held on September 23, 2005, p. 9-10; Transcript of the Hearing held on May 8, 2006, p. 71 line 18 - p. 72 line 25.

49. Furthermore, ORIL has repeatedly stated that on every occasion the price of fresh milk has been increased the demand decreases.[173] ORIL failed to take into consideration that the year 2005 price increase would further decrease volumes for that year making even more unreliable the 2003 volume numbers used for year 2005 price determination and rate of return calculations.[174]

50. By over-estimating the amount of milk to be sold during the period of the price increase, ORIL was artificially reducing the amount of capital per quart of the fresh milk processors. The application of a certain rate of return to an artificially lowered capital base provides an artificially diminished level of reasonable profit required.[175] By 2005, when the new prices went into effect prospectively, the 2004 decrease in volume of sales had further eroded the capital of fresh milk processors.

51. ORIL uses a 10% rate of return over capital. ORIL has no regulatory parameters for this rate of return and has never conducted a study to determine what that rate of return should be.[176] ORIL's only basis for the 10% rate of return is the 1997 US publication entitled Milk Fact which cited this figure as

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[173] See Defendant's Exhibits S and T; see also Transcipt of the Hearing held on May 8, 2006, p. 7 line 23 - p. 9 line 17.

[174] See Defendant's Exhibit K.

[175] See Transcript of the Hearing held on September 23, 2005, p. 33 lines 17 -23.

[176] See Transcript of the Hearing held on May 9, 2006, p. 120 line 19 - p. 122 line 22.

the national average.[177] The parameter is obviously outdated, stale, and fails to take into consideration the economic conditions of doing business in the market in Puerto Rico after May 2006, when the Bonds of Puerto Rico were considerably devaluated by Moody's.[178]

52. The evidence presented by plaintiffs demonstrates that the average rate of return reasonable for the milk industry in Puerto Rico is the figure around 15%. That evidence was not disputed by ORIL.[179] The Department of Consumer Affairs of Puerto Rico uses a reasonable rate of 15.81% return for gasoline wholesalers in Puerto Rico, also a commodity obviously highly affected by increasing fuel costs and electricity.[180] The court does not question the established fee per se; the error is in not performing a reasonable, timely economic study setting the reasonable rate and the continuing usage of stale data as to rate of return (1997), and further not considering currently doing business in the Puerto Rican market under current economic realities. The court does not hint at any figure as to reasona-

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[177] See Transcript of the Hearing held on May 9, 2006, p. 109 line 18 - p. 110 line 11.

[178] The court takes judicial notice of an economic event which took place in Puerto Rico, is undisputable and has obvious economic repercussions . Further the court is authorized to take judicial notice of events published in the internet. *Chhetry v. U.S. Department of Justice*, 490 F.3d 196, 2007 WL 1759472.

[179] See Transcript of the Hearing held on September 20, 2005, p. 76 line 23 - p. 77 line 4.

[180] See Transcript of the Hearing held on May 9, 2006, p. 110 lines 17-25.

ble rate of return. This rate belongs to the setting by the Administrator, not the court.

53. Prior price orders issued by ORIL have demonstrated year after year that even with the downwards adjustments made by said office to the fresh milk processors' capital base, when actual real numbers were reviewed the following year plaintiffs were never able to obtain even the 10% return over the adjusted base ORIL had estimated they would make.[181]

54. The regulatory system of ORIL has created for the fresh milk processors yearly losses that have consistently diminished their capital base. The normal regulatory way of dealing with this issue is by creating a capital account of "regulatory accrual" that would add to the capital base the erosion experienced because of this regulatory system.[182] By providing in future rates a rate of return over the real capital plus the capital losses, the companies could be made whole and be provided the necessary recovery of cost and reasonable profit. ORIL has refused to recognize a regulatory accrual account as part of the capital base.[183] The last order of ORIL resulting from a yearly price revision was is-

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[181] See Defendant's Exhibits K, S, T and Plaintiff's Exhibit 81 and Transcript of the Hearing held on May 9, 2006, p. 51 line 10 - p. 67 line 21; p. 70 line 2 - p. 74 line 17.

[182] See Transcript of the Hearing held on September 20, 2005, p. 74 lines 6-12.

[183] See Defendant's Exhibit V and Transcript of the Hearing held on November 3, 2005, p. 127 line 25 - p. 129 line 2; Transcript of the Hearing held on May 9, 2006, p. 47 line 11 - p. 48 line 17; Transcript of the Hearing held on September 20, 2005 p. 74 - lines 5-14.

sued on April 19, 2007.[184] Again, this order was issued without first establishing the applicable regulatory parameters. The fresh milk processors' price structure, last determined on the basis of year 2003 sales volumes and costs, remained untouched. This time the Administrator authorized the adjustments allowing discounts to agents and other promotions despite having previously sustained in the court proceedings that the discounts were illegal.[185] The shrinkage factor that the Administrator applied this time is different to the one applied in the order effective May 2005. Despite this, the Administrator again justifies this shrinkage factor by saying that it is the shrinkage factor "historically applied". For the first time, the Administrator adjusted the revenue of the plants by including as income of the regulated fresh milk processing business the income of separate corporations related to plaintiffs, operating in the unregulated plastic business. ORIL did so despite a firm and final judgment from the local court providing that ORIL could only use in its price reviews revenue from fresh milk sales.[186] The critical matter for constitutional repercussions is not a violation of a local court opinion, but that again there is yet another unannounced change in conditions used for the first time against the milk processors. This is yet another change in conditions. The Administration makes no conclusion that

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[184] See Exhibit 12 of Docket No. 446. Please refer to Exhibit 12 of Docket No. 469 for a certified translation of the same.

[185] See Transcript of the Hearing held on May 8, 2006 p. 129 lines 14 - 24.

[186] See Transcript of the Hearing held on May 11, 2006 p.49 lines 17-25; See also Defendant's Exhibit E.

the plastic pricing of plaintiff included in their books is excessive in terms of market availability but adjusts the same nonetheless.[187] Under the new order, the Administrator indicated that he had no available information on increased costs for electricity and fuel although those costs are available from Government agencies in Puerto Rico and is a matter of simply applying the figures to the 2003 figures he is continuously using.[188]

55. By incurring in the regulatory actions described above ORIL, has not allowed plaintiffs to recover costs and make a reasonable profit.[189]

56. The financial situation of the fresh milk business of the fresh milk processors has greatly deteriorated on account of these administrative acts.[190] The fresh milk processor's market share of the fluid milk market of Puerto Rico continues to go down while UHT's market share of that same market continues to grow. Milk is being destroyed at farm level because Indulac can no longer absorb the huge amount of surplus created by the pricing scheme.[191]

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[187] See Transcript of the Hearing held on September 23, 2005, p. 14 line 22 - p. 15 line 4; and May 9, 2006 p. 39 lines 15-24.

[188] See undisputed facts regarding the information available from the Government agencies in Puerto Rico on Docket No. 446.

[189] See Transcript of the Hearing held on September 20, 2005, p. 90 lines 14-16 and p. 90 line 24 - p. 91 line 7.

[190] See Plaintiff's Exhibits 38, 40, 41 and Transcript of the Hearing held on September 16, 2005, p. 65 lines 19-23; p. 66 lines 3-9.

[191] See Plaintiff's Exhibit 111; Transcript of the Hearing held on June 20, 2006, p. 51 lines 5-18.

57. The milk payment fund under the February 2006 order is not now capable of even paying neither for Indulac's loans nor for the FFIL's programs.[192] Worst still, the last liquidations show that the Fund is running short for over $400,000 every two weeks on the money needed to pay the farmers compensation.[193] In other words, the system is deteriorating so rapidly that now even the farmers' payment is jeopardized as Indulac no longer provides money for said purposes because its responsibility is now limited to less than $0.32 per quart of surplus.[194] Despite the fact that in every biweekly period the deficit increases substantially, and that there is not even enough money to pay the farmers, the Administrator has further reduced the cost of milk to Indulac through an order dated April 5, 2007.[195] Pursuant to that order, the price of raw milk used by Indulac to manufacture evaporated milk and powder milk has gone down. In the liquidation period which ended May 2, 2007 the price reduction for Indulac only resulted in reducing Indulac's payment for milk 17.3%.[196] Although Indulac is the only

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[192] See Plaintiff's Exhibits 124-126. See also Exhibits 1-8 of Docket No. 446. Please refer to Exhibits 1- 8 of Docket No. 469 for the certified translation of the same.

[193] See Exhibit 1 of Docket No. 463.

[194] See Transcript of the Hearing held on March 2, 2006, p. 132 line 14 - p. 133 line 20; Transcript of the Hearing held on May 9, 2006, p. 141 line 11 - p. 149 line 25; Transcript of the Hearing held on May 10, 2006, p. 10 line 6 - p. 11 line 9.

[195] See Exhibit 11 of Docket No. 446. Please refer to Exhibit 11 of Docket No. 469 for the certified translation of the same.

[196] See Exhibit 8 of Docket No. 446. Please refer to Exhibit 8 of Docket No. 469 for the certified translation of the same.

entity in Puerto Rico presently manufacturing those products, the fact that the order makes it clear that said pricing will be available only to Indulac eliminates any incentive to the fresh milk processors to proceed with the manufacture of the same.

58. The Administrator has also allowed the fresh milk processors to buy milk for certain by-products uses at below the level of 66.125 cents. This has had a very limited impact in reducing the fresh milk processors contribution to the payment Fund. This is the case as the amount of milk for by-products in the case of plaintiffs is not substantial. Furthermore, in the case of Suiza the amount of milk that Suiza is now buying at below 66.125 cents is an amount of milk that Suiza previously imported as powder milk.[197] Suiza is therefore now contributing higher amounts to the payment Fund than before because it is buying in Puerto Rico milk that it used to import as powder milk. The price reduction to Suiza, as proffered by Suiza, pursuant to the liquidation of May 2, 2007, amounts to less than one cent from the 66.125. On the other hand, the reduction granted to Indulac for evaporated milk, powdered milk and cheese is 5.5 cents from 32 cents per quart. Indulac's percentage price reduction is around 17.5% as compared to 1.3% for Suiza. (See Docket 446, Ex. 8, and Translation at Docket 469.)

59. ORIL has attempted to maintain the fresh milk price to the consumer as low as possible in order to make that staple readily available. This is a valid

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[197] See Exhibit 8 of Docket No. 448. Please refer to Exhibit 8 of Docket No. 464 for the certified translation of the same.

public policy and also prevents the decrease in demand that accompanies high prices. However, at the same time, ORIL has been squeezing the fresh milk processors preventing them from recovering reasonably incurred costs and making a reasonable profit by forcing them to operate with the insufficient margin between an artificially high cost for raw milk. This creates an artificial capital credit in that fictitious stale sales of milk are calculated in the formula and results in a mistaken price to plaintiffs' clients.[198]

60. The procedure in its totality is designed to allow Indulac to purchase raw milk well below cost without affecting the farmers' income. With this below cost milk, Indulac competes against both the fresh milk processors and the importers of UHT milk.

61. As admitted by the Administrator of ORIL, Mr. Pedro, and the Chief Executive Officer of Indulac, Mr. Benitez, without a much below cost price for its raw milk Indulac would not be able to compete with imported UHT.[199] When Indulac requested in December of 2006 a further decrease in pricing for raw milk; the UHT sole local producer openly admitted that it needed additional price accommodations in order to be able "to compete with importers of UHT milk."[200] Indulac controls most of the

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[198] See Transcript of the Hearing held on September 20, 2005 p. 8 lines 11-17 and p. 9 lines 6-7.

[199] See Transcript of the Hearing held on February 27, 2006, p. 34 line 19 - p. 35 line 3.; Transcript of the Hearing held on June 19, 2006, p. 76 lines 2-17.

[200] See Exhibit 1 of Docket No. 448. Please refer to Exhibit 1 of Docket No. 464 for a certified Translation of the same.

UHT market of Puerto Rico because of its well below cost price for raw milk. Without the economic benefit, not available to importers, the importers would take over the UHT market in Puerto Rico.[201]

62. The FFIL has as one of its most important roles, the promotion of the consumption of fresh milk.[202] The FFIL has indicated that fresh milk is preferable to UHT for health reasons.[203]

63. Puerto Rico in the last years has not produced enough fluid milk to satisfy yearly local fluid milk demand.[204]

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[201] See footnote 5 at p. 2 of Exhibit 1 of Docket No. 448. Please refer to Exhibit 1 of Docket No. 464 for a certified translation of the same.

Facts Nos. 26, 40, 59, 60, 61 and 65 are critical to the remedy under the Dormant Commerce Clause. The facts are the establishment by application of a regulation of a price scheme only applicable to the only manufacturer of local UHT. Indulac is authorized to purchase raw milk at well below cost price of the dairy farmers financed by the fresh milk processors who ultimately pay more than required. The procedure allows the local producer to favorably compete with the UHT importers. The procedure of purchasing raw milk to manufacture UHT, powdered milk, evaporated milk, at well below cost is authorized exclusively to that local producer, Indulac, as the Administrator stated: "Without these two Bills of Law (sic) the imported UHT milk (sic) is going to take over the entire market. . . Further, as admitted by the Chief Executive Officer of Indulac, without the below cost price of raw milk Indulac can not compete with the importers. (See § 26 infra.)

[202] Transcript of the Hearing held on June 6, 2006, p. 5 lines 1-4.

[203] See Exhibits Defendant's Exhibit PP and Plaintiff's Exhibit 118; Transcript of the Hearing held on June 6, 2006, p. 11 line 15 - p. 12 line 23.

[204] See Defendant's Exhibit KK.

64. Classified milk pricing is the system prevalent in milk markets throughout the United States.[205] This system classifies raw milk for the manufacturing of fluid milk at the highest price.[206] No distinction is made between UHT and fresh milk.[207] The years before UHT, Puerto Rico was operating under a classified pricing system allowing the purchase of raw milk for milk by-products to be paid at a lower price than milk for fluid milk manufacturing.

65. In no jurisdiction of the United States is a fresh milk processor required to pay a price well above cost and profit for raw milk so that a local UHT producer can pay much less than cost and profit for the same raw material. The purchasing scheme allowing the exclusive UHT local manufacturer to purchase raw milk well below cost of fresh milk prices and below cost of the dairy farmers allows the local UHT manufacture to compete favorably with the importers.[208]

66. At the end of 2006, Indulac was requesting from ORIL a reduction in the price of raw milk paid by

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[205] See Kenneth W. Barley, *Marketing and Pricing of Milk and Dairy Products in the United States*, Iowa State University Press, 1997, page 118; Transcript of the Hearing held on September 16, 2005, p. 41 line 24 - p. 42 line 5.

[206] See Transcript of the Hearing held on August 22, 2005, p. 74 line 24 - p. 75 line 5; p. 77 line 7; Transcript of the Hearing held on September 26, 2005, p. 36 line 20; p. 37 line 4.

[207] See Transcript of the Hearing held on September 16, 2005, p. 41 lines 19-24.

[208] See Transcript of the Hearing held on August 22, 2005, p. 75, lines 22-25.

Indulac.[209] Indulac was further requesting to be relieved of the obligation to pay for the amount of milk that is now destroying at the farm level.[210] In the year 2006, this amounted to more than 7.7 millions quarts.[211] Furthermore, Indulac requested the Administrator that it be allowed to pay for any milk received over 83 million quarts according to the final rentability of that milk.[212] The last liquidations of the year 2007 reflect that Indulac is not paying for destroyed milk.[213] Indulac, as well as the other participants in the market, has been operating to maximize its profits.

67. During this year the biweekly money available to pay the farmers is running short by several hundred thousand dollars per biweekly period, reaching the highest deficit ($726,212.84) in the biweekly period of May 30, 2007. In the last biweekly period that shortage to pay the farmers was of over $600,000.[214]

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[209] See Exhibit 2 of Docket No. 448. Please refer to Exhibit 2 of Docket No. 464 for a certified translation of the same.

[210] Id.

[211] See p. 2 of Exhibit 1 of Docket No. 448. Please refer to Exhibit 1 of Docket No. 464 for a certified translation of the same.

[212] See Exhibit 11 of Docket No. 446. Please refer to Exhibit 11 of Docket No. 469 for the certified translation of the same.

[213] See Exhibit 1 of Docket No. 463.

[214] Ex. 1 of Docket No. 474.

## ESSENTIAL FACTS AS TO DUE PROCESS, EQUAL PROTECTION AND TAKINGS CLAUSE VIOLATIONS

1. The Administrator of ORIL has created a price scheme wherein the local manufacturer of UHT purchases raw milk at below cost of production of the dairy farmers while the milk processors, in order to make up the economic deficit, must pay substantially over cost and reasonable profit rates for the same raw milk.

2. The milk industry in general is regulated at the level of dairy farmers' price as to the price paid by the two milk processors for raw milk and at the price paid by the fresh milk consumers. UHT is regulated in Indulac's favor as to the price paid for the fresh raw milk to the dairy farmer. The UHT milk is not regulated at the price to the consumer.

3. For many years, the fresh milk producers have been financing the low cost of raw milk paid by the UHT local manufacturer.

4. The UHT manufacturer is not audited by ORIL as the two fresh milk processors are audited.

5. Notwithstanding the legal requirement of auditing the entire milk market in Puerto Rico, for years the only parties actually being regulated are the fresh milk industrial processor as well as the dairy farmers. The dairy farmers are technically regulated with a price of milk sold to the milk processor and a price for UHT and other milk products sold to Indulac. However, said price for years has been unilaterally increased by Indulac, a government-controlled

entity who in turn is controlled by the dairy farmers. Indulac is not regulated as to the price of fresh milk to consumers and receives raw milk at extremely low, below cost prices.

6. The Administrator set new prices for Indulac in February 2006 for purchase of raw milk at $0.32 per quart for fresh milk without a hearing and granting in only one week exactly the price requested by Indulac. Further, Indulac is permitted by administrative inaction to unilaterally increase the price it pays to the farmer.

7. Indulac was partially relieved by the order of February 2006 of paying loan payments and programs paid to Fund (FFIL) previously by Indulac for the well being of the milk industry; the program then was being paid by Indulac and the milk processors. Said order again decreased the price of fresh milk to be actually paid by Indulac.

8. Indulac was relieved of payment through the order of February 2006 of the economic burden of having to increase payment of milk (to stabilize farmers' income) as the demand of fresh milk continued.

9. The order of February 2006 continued the price of raw milk paid by fresh milk processors to dairy farmers at 0.66125 and set the recovery cost and profit of dairy farmers at 0.55 per quarts, while Indulac's price was set at 0.32 per quart (plus Indulac relieved of prior obligations as set at § 7 and 8 supra).

10. By order of April 5, 2007, the Administrator granted a further reduction to Indulac in its net payment of raw milk to dairy farmers of $0.32. Milk used by In-

dulac for the production of evaporated milk was reduced to $0.12 as well as powdered milk to $0.12. Raw milk used by Indulac to produce cheese is to be purchased at $0.20. The net result is that the price of raw milk to Indulac is now reduced to $0.265 (as calculated by Suiza). Said reduction in prices is not authorized for the two fresh milk processors.

11. Similarly, fresh milk processors were granted a moderate decrease in purchase price of raw milk destined for certain milk by-products, mainly powdered milk. However, the amount constitutes in total a decrease of less than one cent from the price paid of 66.125. The reduction, as calculated by Suiza, to Indulac is substantial since the diminishment of the price constitutes 5.5 cents less than the 32 cents paid for a quart. The final result is that the price reduction for Indulac constitutes around 17.5% as compared to 1.3% reduction to Suiza.

12. The price scheme has caused substantially, or at least partially, a considerable loss in the market of fresh milk and a considerable increase in the UHT market to the point that Indulac has ceased to be a "balancing plant," a tamed "toothless" tiger, to purchase excess milk produced by the dairy farmers and is now an aggressive competitor armed with an economic regulatory formula that allows purchase of its principal raw material at much less than one half the payment made by the two fresh milk producers. The sales of fresh milk from 1998 to 2004 have decreased 2.4% per year for a total reduction of 14%. On the other hand, the sales of UHT have increased during

the period at the rate of 10.5% per year for a total of 82%. (See Exhibit 29.)[215]

13. Suiza has been denied by ORIL a permit to operate an UHT processing plant, a determination which has been repeatedly reiterated by dairy farmers.

14. The Administrator of ORIL is ordered to "at least once a year" perform the necessary adjustments according to the increase and/or reduction of the production costs, as well as operational expenses at all levels, and to review the price of milk purchased from the dairy farmers as well as the price of finished fresh milk produced by the industrial process. P.R. Laws Ann. Tit. 5 § 1107 (a)-(e). The Administrator failed to comply with his obligation in one year, alleging a change in ownership and/or control of Suiza. Said exception is not authorized by any statute, creating de facto a presumption of illegality as to Suiza due to a change in stock ownership and prejudiced the other milk processor, Tres Monjitas.

15. ORIL has no mechanisms in place for automatic price adjustments (higher or lower) based upon recurring production costs necessary for both the dairy farmers and/or the fresh milk processor. (Indulac does not have their price to the consumer regulated.) There are certain costs that are critical and recurrent wherein the matter can be easily handled, ie. fuel costs, electricity cost, labor costs, resin, food, grain costs, and supplements for the cows.

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[215] Total sales of UHT in 1998 were 38.40 million quarts and in 2004, 69.93 million quarts. (Ex. 29); fresh milk had a market of 318.50 million quarts reduced to 275.27 million quarts for 2004 (See Ex. 28-30).

16. There is no mechanism in place for the milk processors and dairy farmers to recuperate the losses on the basis of higher costs basis that occur from year to year. There is simply no regulatory accrual to recuperate interim losses that occur from one year to another. There is, therefore, no remedy to recuperate for past losses. The Administrator has made no adjustment to mitigate for the losses of the milk processors from year to year that occur either by an increase in cost or as result of a loss in market.

17. The Administrator uses stale 2003 figures of the milk processors to determine 2005-2007 costs and also to determine a reasonable process to the consumer of the finished fresh milk and to determine a reasonable profit for the industrial milk processors. Equally, in using sales to the public figures that are stale even though recent figures are available (2004 for price set in 2005), the Administrator uses said figures even though the market of sales has actually declined in the case of fresh milk market. In using stale figures, the Administrator uses said figures and fictitiously increases the capital of the milk processors and further fictitiously considers sales that are below actual sales.[216]

18. Using stale sales figures of 2003, as was the case of the price order of April 2007, is particularly prejudicial since the volume of sales of the fresh milk processors has decreased (as is known to the Administrator) during said period by around 10%. Further, that the costs of certain critical production costs such

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[216] The court does not understand the use of stale sales figures since the Administrator has actual sales at least every quarter of a year.

as electricity and fuel have undoubtedly increased are matters of public knowledge[217], and are consequently readily available. (The Administrator alleges that these figures have not been provided—notwithstanding the figures are public and can be simply adopted and applied to the 2003 figures being reiterately used by ORIL as to the two processing plants.

The rules of cost analysis are constantly being changed from year to year, sometimes directly in contradiction, some are added, some are eliminated, all to the detriment of the fresh milk processors and without any notice whatsoever. The court provides highlights.

A) Other non-related Business — In the April 2007 price review the milk processors profit in other non dairy markets (juices) was taken into account as a profit for the first time notwithstanding said criteria never before having been applied. Further, there exits a prior court final decision to the contrary holding that profits of non regulated businesses would not be taken into account. The legal issue for federal due process purposes is not that there is a violation to a local judicial decision, but that this parameter was unannounced and retroactively applied creating due process concerns.

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[217] Fuel costs are regulated by the Consumer Affairs Department and electric costs are public since the electricity is provided by a public government corporation.

B) Price Discounts — Price discounts in considerable dollar amounts have been unchallenged by the Administrator of ORIL as to Indulac. The position of the Administrator relating to discounts as to the fresh milk producers has been in constant flux and outright contradiction. During the review of 2005, the Administrator bluntly denied any type of discount to agents and/or for other promotions. Prior thereto they had been at least partially allowed. In 2005 without making any conclusion as to any antitrust and/or price discrimination violation the discounts were deemed "illegal." Yet in the past the Administrator allowed some discounts yet rejected others. Notwithstanding, similar discounts in the amount of 1.8 million dollars were allowed to Indulac in 2006 and Indulac also claimed additional discounts due to inventory obsolescence in 2006. In April 2007, the Administrator surprisingly allowed discounts without stating any reasons whatsoever. Notwithstanding, the milk processors have lost any and all credit from the year 2005 until 2007 and have yet to have a defined parameter.

C) Returns of Product — During 2005 the Administrator changed the rules as to income from sales of fresh milk. In the past, any amount of monies genuinely proven returned to clients for the product were not counted as income. In 2005, returns for the first time were not included as a credit and hence total sales were fictitiously in-

creased as milk returns were rejected without any reasoning whatsoever. Again there was no defined parameter.

D) Shrinkage constitutes the loss of milk inherent to any milk manufacturing process. The principal factor causing shrinkage is temperature. For the first time in the price order of 2005 the Administrator made a reduction in the allowance of shrinkage factors. The Administrator alleged "historical" factor figures as to the change. At the hearings in court the reasoning was not proven. The low factor authorized was not proven to be "historical." See Finding of Fact #45. The shrinkage factor claimed by the fresh milk processors in court compares favorably with average shrinkage factors in geographic parallel regions in the Continental United States less affected by heat. In the year 2007 the historical factor was changed again without providing any reasoning. Again the court notes the lack of standards and/or of applying standards at random or not being rationally set.

E) Plastic Container cost and professional fees. The Administrator uses constantly for cost analysis the lower figure presented by either of the two plants for plastic containers and professional fees independent of the legitimacy of either plants actual legitimate numbers.

ORIL'S disallowance as to cost of professional fees as to price regulations

without making any findings or providing reasoning seems, at best, arbitrary.[218]

F) Cost analysis using stale sale figures.

The use of 2003 figures and/or of long past years overstates the amount of milk sold as the evidence provides a clear market loss by the fresh milk producers. ORIL is hence artificially reducing the capital per quart of the fresh milk processor (stated otherwise the capital of the milk processors is also artificially increased since it deems sales for interim years as made and profit realized when said calculated profit was never materialized as wrongful sales figures are applied.) The error is simply in that actual sales are not those reflected in past years since sales of fresh milk are decreasing in alarming numbers. The court does not understand said use of stale figures since ORIL has updated sales at least up to the last quarter of the current year.[219] [219] The application to a certain wrongful sales figure to a rate of return per quart lowers the capital base and results in a diminished level of profit.

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[218] At worst it is vindictive since the determination to deny professional fees was made after the hearings in the instant injunctive hearing began. Anyway, there is no reasoning provided by ORIL.

[219] In fact the Administrator has updated figures as to raw fresh milk sales up to the last fifteen day monthly liquidation of the current year. The liquidation of the last fifteen days of June 2007 is currently available.

G) Cost analysis using stale cost figures. Using stale cost figures further breeds mischief as to the final result. As stated herein it is unquestionable that certain critical costs have increased in Puerto Rico since 2003 as to at least electricity and fuel costs. Placing outdated 2003 figures into this category will obviously yield an artificial, unfair result to the real costs of the fresh milk industrial processors, Suiza and Tres Monjitas.

H) Rate of Return (Profit)

The rate of return is 10%, which is the average rate of return for the milk industry in the Continental United States for the year 1997. The parameter even when instituted and now questioned, is not based on any study as to where Puerto Rico fit into the 1997 national U.S. average. Further, it is now stale and fails to take into consideration the economic conditions of doing business in Puerto Rico, particularly after May 2006 when the Bonds of Puerto Rico where considerably devaluated by Moody's.[220]

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[220] The court takes judicial notice of an unquestioned economic event which occurred in Puerto Rico, the devaluating of Puerto Rican Bonds by Moody's occurring in May 2006 as reprinted in internet articles describing and confirming the event. *Chhetry v. U.D. Department of Justice,* 490 F.3d 196, 2007 WL 1759472 (CA 2). (". . . The BIA did not err in taking administrative notice of changed country conditions [current events] based on articles found on Yahoo.com or the web sites of CNN and BBC News") (citing *Hoxhallari v. Gonzales*, 468 F.3d 179, 186 N.5 (2nd Cir. 2006).) The court

## FACTS PARTICULARLY CRITICAL AS TO THE CLAIM UNDER THE DORMANT COMMERCE CLAUSE

As a preliminary matter the court reiterates an emphasis on economic reality as to this case. Indulac, the exclusive UHT manufacturer in Puerto Rico, is a public corporation now controlled by the dairy farmers as opposed to a corporation with participation by the fresh milk processors as was in the past. The FFIL is also exclusively controlled by the dairy farmers (five Board members out of nine) and is an entity dedicated to "promoting the production, sale, processing, and consumption of fresh milk and its by products and any other activity for the advancement of the milk industry." P.R. Laws Ann. Tit 5 § 1099. The dairy farmers, therefore, control both the FFIL and Indulac and can therefore create plans to promote UHT, exclude Indulac from payments to certain programs, obligate fresh milk to contribute by themselves for certain other programs and

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has found at least three articles in the web published at USA Today.com published May 8, 2006 entitled "Puerto Rico Bond cut to near junk"; an article published at NY Times.com entitled "Puerto Rico's woes lead to Protest and fears of worsening financial Fallout" published May 8, 2008; and an article published at www.free republic.com entitled "Puerto Rico Government shut down: Bonds became junk," published on May 8, 2006, all reiterating the reality that Moody's had down graded Puerto Rico credit by degrading 4 (four) billion dollars in bonds and describing the degrading matter as a "fiscal crisis."

Further, the matter being taken as judicial notice by the court is authorized at preliminary injunction level hearing notwithstanding its hearsay contents. *Asseo v. Pan American Grain Company, Inc. Et al.*, 805 F.2d 23, 26 (1st Cir. 1986) ("Affidavits and other hearsay materials are often received in preliminary injunction proceedings).

above all can manipulate the price of raw milk to be paid to themselves thru Indulac, as they have actually done, notwithstanding regulation from the Administrator.

The dairy farmers oppose allowing fresh milk processors to manufacture fluid milk in UHT form. The dairy farmers have in the past and throughout the injunctive proceedings attempted to purchase the fresh milk processors. The dairy farmers have attempted to control the entire market including the milk processors, the FFIL and Indulac. Those efforts entail the participation of officials of the Government of Puerto Rico involved directly and indirectly in the milk industry and price setting scheme. The more desperate the financial condition of the two fresh milk processors, the easier for the two dairy farmers to acquire them or eliminate them. The dairy farmers thus de jure hold the reigns of power in the industry.[221] Under this factual scenario as to the actual power of the dairy farmers the court sets forth the facts relative to the violation of the Dormant Commerce Clause. (See generally Finding of Fact No. 8.)

ORIL has developed a sophisticated price scheme authorizing for years the only UHT local manufacturer, Indulac, to purchase raw milk at well below cost production price and reasonable profit to the dairy farmers compared to the price paid by fresh milk producers. The below cost price established by regulation is financed by the fresh milk processors who are obligated to pay by regulation a much higher price in order to offset the below cost sale to the UHT milk producer. The purpose is to enable the UHT producer to favorably compete with

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[221] The Administrator of ORIL was formally the Chairman of the Board of Indulac, now a Director and receives indirect compensation by the payment of the car used and other expenses for the FFIL.

the UHT importers and to compete with the fresh milk processors. The deal of purchasing fresh raw milk in below cost fashion to manufacture UHT is only available to local UHT manufacturer. The Administrator of ORIL stated at the injunctive hearing: "Without these two Bills of Law (sic) the imported UHT milk (sic) is going to take over the entire [UHT] market." Further, the Chief Executive Officer of Indulac openly admitted that without the below cost price of raw milk, Indulac can not compete with the importers. See Findings of Fact No. 26. See also Findings 40, 59, 60, 61, and 65. Other economic incentives have also been provided to Indulac, such as canceling debts and discontinuing economic contributions to the FFIL, and paying even lower amounts for other by-products of milk in order to even further lower their costs of milk in order to be able to favorably compete with the importers.

Finally, in the House Bill 126 to the Legislative History and Declaration of Purposes of Law No. 34, known as the Milk Industry Regulation Act, codified at P.R. Laws Ann. Tit. 5 § 1092 et sec., the Declaration of Legislative History and Purposes states the following as to the solution to the then chaotic critical situation of the local milk industry relating to the importation of dairy products:

> "(1) Instrument regulation that will allow to dispose of the milk surplus in such a manner that, without affecting the interests of the persons engaged in the operation of the business in the different phases of the industry, the consumer would be provided dairy products that will generally substitute."

Hence, through the milk surplus program back in 1957, "the consumer would be provided dairy products that will gradually substitute imported products." They have evidently complied and set forth the program by over-providing to Indulac, the purchaser of the excess milk, with a program of incentives and economic relief. The regulation now adds purchase of cheap raw milk designed to fight the importers and now fifty years later to be an aggressive competitor of the two plants taking considerable part of the market to the point of enabling the purchase of the two plants at less than their economic value.

The Administrator has not instituted a neutral program as to a classified pricing system to compete with the importers, but rather an aggressive program in direct violation to the Milk Industry Regulation Act to provide undue advantage to the local manufacturers over importers and to be to curtail the fresh milk market and increase its UHT market.

## JUSTICIABILITY

Before entering on the merits the court deems appropriate to dispose of potential justiciability doctrines resulting from the interpretation of Article II, § 2, of the United States Constitution as to "cases" and "controversies." The United States Supreme Court in the past has reiterately stated that the justiciability requirement as to "case" and "controversy" imposes substantial constitutional limits on the federal judicial system. Further, other justiciability requirements are derived not from the Constitution but from prudent judicial administration. These last doctrines are turned "prudential." The prudential requirements are self-imposed by the Supreme Court and may be overriden by Congress. *Warth*

*v. Seldin*, 422 U.S. 490, 501 (1975) (Congress may grant an express right of action to persons who otherwise would be barred by prudential standing rules). These principles are related to justiciability. First, the justiciability doctrine is related to separation of powers. *Flast v. Cohen*, 392 U.S. 83, 95 (1968). Second, the doctrine of justiciability serves to "conserve judicial resources." Federal Jurisdiction, Erwin Chemerisnky, 4th Edition Aspen Press. 2003, p. 45. Third, the doctrines of justiciability are geared to impose judicial resolution making by providing "the federal courts with concrete controversies best suited for judicial resolution." Id., p. 46. See also *Flast v. Cohen*, 392 U.S. at 85. This principle ensures that concrete controversies and proper litigants are before the court. *Baker v. Carr*, 369 U.S. 186, 204 (1962). Finally, the justiciability doctrine presents "fairness especially to litigants that are not properly before the court." Chemerinsky, p. 46.

The court has paused to examine the prudential doctrines' requirements since there exists a challenge of defendant specially as to "standing," particularly as to the Dormant Commerce Clause cause of action claimed by plaintiffs.

The case is obviously ripe since the regulations challenged, in an applied fashion by plaintiff, are in effect. Some had been in place since years prior to the challenge, others were enacted prior to the filing, and others enacted and applied after the case began, and finally others have been established after the close of the hearings. The application of the regulation, hence, is a final decision of the regulatory agency and is ripe for a challenge under the Due Process, Equal Protection and Takings Fifth Amendment Clauses and/or the Just Compensation Clause. *Williamson County Regional*

*Planning Com'n v. Hamilton Bank*, 473 U.S. 172, 186, 105 S. Ct. 3116 (1985) ("a claim that the application of government regulations effects a taking of property interest is not ripe until the government entity charged with implementing the regulations has reached a final decision regarding the application of the regulation.") The quoted threshold has been met in the instant case.

Plaintiffs have obvious standing to challenge the regulations issued by ORIL since a price is set to them as milk processors as to the purchase of raw milk from the farmer. Further, a price of sale to the consumer is established resulting from the challenged regulations. Hence, the court must conclude as to the Due Process, Equal Protection and Taking Clause challenge that plaintiffs have standing under *Baker v. Carr*, 369 U.S. at 204-208.

There is, further, a challenge under the Burford[22] abstention doctrine. However, Burford does not apply "when the effect of an entire state regulatory scheme is challenged as unconstitutional." *Tenoco Oil Company v. Department of Consumer Affairs*, 876 F.2d 1013, 1029 N. 23 (1st Cir. 1989). The court understands that this boundary has been met as plaintiffs are challenging the price paid to the consumer; the parameters used by the Commissioner, the change in parameters, the use of stale figures, the lack of regulatory accrual to recuperate interim losses; the low price of raw milk paid by UHT manufacturer, Indulac, all financed by the milk processors; the use of a fair return rate figure to the milk processors set forth in 1997 from an average United States Continental figure applicable to the Puerto Rican market in 2005-2007.

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[22] *Burford v. Sun Oil Co.*, 319 U.S. 315, 63 S. Ct. 1098 (1943).

Plaintiffs are hence challenging the entire regulatory scheme as applied and hence there is no *Burford* abstention as counseled by the First Circuit Court in *Tenoco Oil*, Id.

## APPLICABLE LAW AND DISCUSSION

### a. Due Process, Equal Protection and Taking Clauses.

#### *Due Process and Equal Protection Clauses*

The Due Process, Equal Protection and Taking Clauses unquestionably apply to Puerto Rico. *Tenoco Oil Company, Inc. v. Department of Consumer Affairs, et al.*, 876 F.2d at 1017 n.9. In *Tenoco*, the plaintiffs alleged that the orders issued by the Secretary of the Department of Consumer Affairs regulating the gasoline prices violated constitutional and statutory provisions of Puerto Rico law, as well as the due process and taking clauses of the United States Constitution. The Court of Appeals stated as follows:

> The Supreme Court has held that one or another or both of the Constitution's two due process clauses (that in the Fifth Amendment and that in the Fourteenth) apply to Puerto Rico even though the latter is not a state. *Calero-Toledo v. Pearson Yacht Leasing Co.*, 416 U.S. 663, 668-69 n.5, 94 S.Ct. 2080, 2084-85 n. 5, 40 L.Ed.2d 452 (1974).
>
> The Supreme Court has not ruled definitely on the application to Puerto Rico of the takings clause of the Fifth Amendment, which provides that "private property [shall not] be taken for public use without

> just compensation," U.S. Const., Amend. 5. *But see Webb's Fabulous Pharmacies v. Beckwith*, 449 U.S. 155, 159, 101 S.Ct. 446, 449-50, 66 L.Ed.2d 358 (1980) ("takings" clause incorporated into the Fourteenth Amendment, applicable to the states). We have no doubt, however, that the takings clause, like the due process and equal protection clauses, applies to the Commonwealth of Puerto Rico. *See, e.g., Culebras Enterprises Corp. v. Riv. a Rios*, 813 F.2d 506 (1stCir. 1987) (assuming applicability). *See generally* J.R. Torruella, *The Supreme Court and Puerto Rico: The Doctrine of Separate and Unequal* (1985).

*Tenoco Oil Co.*, 876 F.2d at 1017, n. 9.

As to the question of whether the gasoline prices regulation [milk price regulation] being challenged violates the takings and due process clauses, the appellate court held that "[a] regulation takes property without due process of law only if "arbitrary, discriminatory, or demonstrably irrelevant to the policy the legislature is free to adopt. . . " *Tenoco Oil Co.*, 876 F.2d at 1021 (citing *Pennell v. City of San Jose*, 485 U.S. 1, 108 S. Ct. 849, 857, 99 L. Ed. 2d 1 (1988) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 769-70, 88 S.Ct. 1344, 1361, 20 L.Ed.2d 312 (1968) (quoting *Nebbia v. New York*, 291 U.S. 502, 539, 54 S.Ct. 505, 516-17, 78 L.Ed. 940 (1934). The regulation will stand if a rational relationship exists between it and a legitimate governmental objective. *Tenoco Oil Co.*, 876 F.2d at 1021; *Nebbia*, 291 U.S. at 537, 54 S.Ct. at 516. *See also PFZ Props. Inc. v. Rodriguez*, 928 F. 2d 28, 31-32 (1st Cir. 1991).

A similar analysis governs regulatory classifications under the Equal Protection Clause. *Medeiros v. Vincent*, 431 F. 3d. 25, 32-33 (1st Cir. 2005) (citing *Eastern Enterprises v. Chater*, 110 F. 3d 150, 159 (1st Cir. 1997)) ("[A] court must apply substantially the same [rational basis] analysis to both substantive due process and equal protection challenges"). To meet the constitutional requirements, a regulation must rationally pursue a legitimate governmental interest. The government, however, cannot pursue its interest(s) in an arbitrary manner.

In the instant case, the milk regulatory scheme appears to be defective, as it only purports to pursue a legitimate state interest without first establishing a rational nexus between the basis for the regulation and the governmental legitimate interest. As stated above, the enacted regulations are primarily relevant to a policy that ORIL was indeed impaired to pursue. The ultimate result, however, is two-fold as the regulatory scheme has an adverse impact on plaintiffs, the milk industry and the consumer.

The milk regulatory scheme has forced plaintiffs to "subsidize" now a strong competitor, Indulac, by providing this governmental entity a distinct edge over its mainland competitors in the market of the UHT milk to benefit those in control of Indulac, that is, the dairy farmers. The regulatory scheme provides UHT a significant advantage by granting Indulac the right to purchase the raw milk below the cost of the dairy farmers to compete against the **fresh milk producers**, and the evidence reveals a high market increase by UHT and a declining market obtained at least partially by the low cost of pricing the raw milk. Further, the farmers also obtain the purchase of all within quota of their dairy production, and most critically have expressed their continued inter-

est in purchasing the fresh milk processors. The economic value of milk processors is in continued decline resulting at least partially from the increased UHT market created by the purchase of financed low priced raw milk by the milk processors who are forced to pay higher prices to the dairy farmers to offset the low price paid by Indulac.

The Court notes, however, that the current subsidy program also serves a local or state interest, as it eliminates the cost advantages of the out-of-state producers in a potential violation of the Dormant Commerce Clause.

Puerto Rico, as many other jurisdictions in the United States, has a legitimate state interest in promoting the local milk industry and the consumption of derivative milk products produced locally. Puerto Rico also has a legitimate interest in protecting the employment opportunities created by both the dairy farmers and the processing sectors of the milk industry. However, the state must pursue this legitimate interest within the boundaries set forth by the Equal Protection, Due Process and Takings Clauses, as well as the Dormant Commerce Clause, which are all fully applicable to Puerto Rico. A discussion on the applicability of the dormant Commerce Clause to Puerto Rico is discussed under a separate sub-title.

As stated above, the Government of Puerto Rico has a legitimate interest in promoting the consumption of fresh milk, particularly the milk that is locally produced. The FFIL, a governmental entity existing to promote the fresh milk consumption, has confirmed that fresh milk is healthier that the UHT milk. However, it appears that there is no rational nexus between the current milk regulatory pricing scheme of raw milk and the alleged

governmental legitimate interest being pursued, as the pricing regulation clearly favors Indulac, the sole processor of UHT milk, and the purchase of subsidized low priced raw milk dwindles at least partially a considerable part of the milk market from the fresh milk processors.

The core of the Puerto Rico milk regulatory pricing scheme is the fixed price of raw milk, which is currently below the production cost, and it is fully controlled and regulated by the defendants, in order to subsidize Indulac, who is an exclusive local UHT milk market participant, and who also is an entity created by the government. As it stands, Indulac is allowed to pay a fixed price below the production cost for the raw milk it uses to produce the UHT milk, in order to compete in the fluid milk market in Puerto Rico, and compete with the UHT importers, their principal competitors. To prevent the dairy farmer from being affected by the low price, the plaintiffs, that is, the fresh milk processors, are required to pay an unreasonable high amount of money, more than double, to allow the dairy farmer to recuperate insufficient costs and make a profit not paid by Indulac. Hence, the price is inflated to the manufacturers of processed milk, and contrariwise sold below cost to Indulac. This scenario causes UHT to increase its market share at the expense of the fresh milk processors. Further, the dairy farmers who control the FFIL and Indulac have openly admitted their desire to purchase plaintiffs' business.

Indulac's principal product is the UHT milk, which is not currently regulated. Indulac, however, is a participant in the regulated fluid milk market of Puerto Rico that obtains the raw material at a subsidized below production cost, and has virtually no restrictions in the free market competition of fluid milk, and it is not affected by the government's milk pricing scheme. Except that

through the challenged regulation, Indulac is able to purchase its principal raw material at an inexpensive price.

The court harbors serious constitutional doubts as to the methodology used by ORIL in seeking to arrive at just compensation. The court briefly explains.

The use of cost and operation expenses used by ORIL. ORIL used 2003 figures as to cost and operational figures where figures were available as to at least half the year of 2004. The stale figures were used in establishing the 2005 pricing regulation as well as the 2006 and the February 2007 pricing regulation wherein the Administrator continued to use the economic figures of 2003. The Court of Appeals in *Tenoco Oil Co.*, 876 F.2d 1013, clearly contraindicated the use of stale figures being used by the Consumer Affairs Department in the establishment of both the "reasonable operational costs" and a "fair return" of the fuel industry. The court stated the following:

> By 1986, the 8.6 cents figure, last used by federal authorities in 1981, was five years old. The federal regulator has regularly used then current nationwide economic data to update their margins, the 8.6 cents figure in 1981 being the most recent product of such efforts. That a figure devised in 1981 for regulating gasoline wholesaler prices throughout the United States and Puerto Rico (taken as a whole) would still be the right one for regulating prices in 1986 in *Puerto Rico alone* is by no means obvious. **One would have expected the agency to be able to support such an essential figure by specific economic data**

> **projecting the wholesalers' reasonable operating costs and a fair return or investment for the year in question, 1986.** (Emphasis ours.)

In the instant case the use of stale figures for establishing the reasonable operational cost and expenses of the milk processors for 2005, 2006[223] and 2007 figures for 2003 were used when 2004 figures were available. The court opines that said regulatory procedure is clearly "arbitrary" within the due process mandate cited at *Tenoco Oil*, 876 F.2d at 1024. Using stale sales figures of the year 2003 as was the case of the 2005, 2006, and 2007 order is particularly prejudicial since the volume of sales of the milk processors is constantly diminishing and said figure is well known by ORIL. During said period the volume of sale of fresh milk was reduced by more than 10%. The use of stale figures further creates a loss in the capital of the manufacturing milk processing plants[224]. As stated above, the use of said stale figures are particularly prejudicial since the use of by ORIL of said figures provides a fictional figure of income and of capital to the two plants given that the volume is clearly fictional as the true sales are diminishing, causing a fictitious credit for the plants in the establishment of the reasonable final profit number of the two manufacturing plants. The reiterated use of fictional, stale, economic figures as to sales

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[223] The price to purchase raw milk from the dairy farmers for the two fresh milk producers in 2006 remained the same at .66125. The price to purchase raw milk by Indulac was reduced to .32 per quart of raw milk.

[224] The fictional profit, of course, alters in turn the reasonable return of capital since ORIL determines the capital base, divides by the number of quarts sold and obtains the capital per quart of milk sold.

volume for the annual price regulation reviews of 2005, 2006, and 2007 constitutes an arbitrary determination in violation of due process. *Tenoco Oil*, 876 F.2d at 1013.

Further, in the year 2005, for the first time, the Administrator adjusted the income in sales by refusing to accept, as in the past was unquestioned, a credit for bonafide returns of milk to the milk process manufacturers. This action created again an artificially higher volume of sales producing an artificial income, another erratic credit within the formula. The problem constitutes not only in an error against the milk processors but also a due process violation in that the change was unannounced and provided no reason or justification for the alteration in the method of calculating sales. Again the determination creates a fiction in the income of the plants as the bonafide credit provided to the consumer or the retailer means that there exists a real unrecognized loss in total sales volumes and income derived therefrom. (No finding was made by the Administrator that the returns were not genuine.) This change in methodology, producing a fictitious higher volume of sales and income, is deemed capricious and arbitrary[225] and banned under *Tenoco Oil*. Id.

Similarly the rules of the regulation are in constant flux and outright contradiction as to allowances for discounts. Prior to the 2005, certain discounts were allowed, partially allowed at random, but no set known parameter was apparent. However, in 2005 **all** discounts were disallowed as to agents and/or for other promotions. In 2005

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[225] The court notes a proclivity of ORIL to changes the rules of the regulation against the plaintiffs almost as if the regulator needed to arrive at a final predetermined price determined through unannounced changes without providing any reasons for the change in parameters.

without making any conclusion of facts and/or any antitrust determination or price discrimination the Administrator banned **all** discounts claimed by the fresh milk processors terming the discounts as "illegal." Notwithstanding, similar discounts were being authorized to Indulac, a competitor in 2006, in the amount of 1.8 million dollars and separately and quietly accepting them as to Indulac due to inventory obsolescence. In the 2007 regulatory review, ORIL authorized discounts from the two plants. No reason was provided. Notwithstanding, the 2005 and 2006 reviews incurred in the error of not allowing discounts, yet the competitor Indulac was allowed discounts corroborated at least as to the review of 2006. Again the regulatory procedure is "arbitrary" in violation of due process requirements under *Tenoco Oil*, Id. As to this particular parameter the methodology of ORIL is also "discriminatory" as to a violation of Equal Protection (competitors not being treated equally by the regulator). *Medeiros v. Vincent*, 431 F.3d at 29.

As stated prior thereto in this order, the Administrator has changed the parameters as to the allowance of loss related to the shrinkage factor in the production of fresh milk. This factor is mostly determined by the temperature of geographic regional area wherein the fresh milk is processed. For the first time, at the regulation process of 2005, the Administrator lowered the shrinkage factor alleging a "historical" factor; plaintiffs proved otherwise in unrebutted fashion. The shrinkage factor was lowered in the regulatory review of 2005 to 0.0075 which used a lower factor that had never been applied. No reason was provided; only a fictional "historic" reason was provided. The Administrator failed to prove that a study on shrinkage had been performed. The shrinkage factor claimed by plaintiff is favorable compared to shrinkage in parallel regions in the Continental

United Stated less affected by temperature. In the 2007 regulatory revision the "historically" applied factor changed to 0.0088. Again no explanation was provided. Notwithstanding, the price reviews of 2005 and 2006 were made with yet another parameter changed and lowered causing prejudice to plaintiffs without any explanation from ORIL. Again the court must conclude an arbitrary determination in violation of due process.[28]

The cost of plastic containers and professional fees should have been accepted in the normal cause of examination as production costs of the final product delivered to the consumer (plastic containers/caps) as well the operational costs of professional fees. Notwithstanding, the administrator used the lowest figure as to each cost item of each individual plant. ORIL had no evidence that Suiza was overpaying plastics nor that there was overpayment by Tres Monjitas as to professional fees. In this particular case the conduct seems to the court irrational and not justified without making particular findings as to inflated costs by either plant. The same occurred with expert fees as to rate regulation proceedings required by law carried on by ORIL. P.R. Laws Ann. Tit 5 § 1107(e) (rate reviews "once a year" and market analysis "at least every four years)." The Administrator denied this operational expense notwithstanding the necessity of both plants to be prepared with economic, marketing and legal experts to present their interest before ORIL. See generally *Driscoll v Edison Light & Power Co.*, 307 U.S. at 120-121 (allowing professional expenses as operational

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[28] Curiously at the hearing of June 30, 2006 it was admitted that the shrinkage factor of Indulac was 8% and that of the plants was around 1% — Tr. June 30, 2006, p. 55-57. The Administrator of ORIL made a similar admission at the hearing of May 8, 2006, p. 116-119 stating the shrinkage factor of Indulac at 8%.

costs as well as expert fees.). Said action by ORIL is arbitrary[27] under the doctrines of *Tenoco Oil*, 876 F.2d at 1021.

The rate of return of capital has been incorrectly determined by ORIL by using stale figures. ORIL uses the 1997 Continental national average to determine "fair return rates or investment" of 2005, 2006, 2007. However, there is no study of the local market to determine how Puerto Rico "fits" into the national average. Second and most critical, a study of 1997 is being used to determine reasonable rate of returns in 2005, 2006, 2007. The Court of Appeals clearly counseled as to the use of stale statistics in rigorously regulated markets:

> "One would have expected the agency to be able to support such an essential figure [devised in 1981] by specific economic data projecting the wholesalers' reasonable operating costs and a fair return of investment **for the year in question,** 1986." *Tenoco Oil*, 876 F.2d at 1024.

The message is quite clear — the regulating administrative agencies may not use stale figures and/or economic studies that are clearly not current. Again the court must find that the fair return or investment rate established at 10% is clearly arbitrary on two grounds, stale and lack of nexus between the Continental average and Puerto Rico in the sense that it is unknown where

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[27] Again the court does not understand the refusal to accept professional fees and/or the retaining of experts as part of operational cost which is traditionally accepted in the price regulation scheme. The specter of a predetermined result raises as these types of traditional operational cost previously unquestioned are unexpectedly denied without any finding whatsoever.

Puerto Rico "fits" within the national average. Finally, in this particular era wherein price of electricity and fuel has undoubtedly raised pursuant to public figures maintained by the Consumer Affairs Department and the government controlled Electric Power Agency and after the significant devaluation of Puerto Rican Government Bonds, the market of Puerto Rico must be thoroughly analyzed to determine the real costs of doing business in Puerto Rico and the economic realities of doing business in the island in 2007 rather than merely applying average rates of return of 1997 in the Continental United States. The use of fuel and electricity costs dating back to 2003 suffers equal infirmity as the use of 1997 figures of rate of return applied to 2005-2007 price regulations.. Again the court must conclude that the "reasonable rate of return or investment" set forth by ORIL is "arbitrary" for the reasons set forth herein.[28]

The law requires ORIL to at least "once a year" review the price regulations. However, there is no regulatory accrual for losses from one year to another. That is losses that occur from one year to another are not accrued allowing for the loss incurred in a past year in a regulated market to be recuperated. A loss to the processing plants is inbued in the pricing system by the decrease in sales of fresh milk from year to year; notwithstanding yet the regulator uses past years sales which are higher than actual sales. The same occurs with electricity, fuel costs that have undoubtedly increased in the last four years but ORIL uses 2003 figures. The Ad-

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[28] The companies suggested a rate of return or investment similar to the rate of return granted by the Consumer Affairs Department of Puerto Rico recently to the fuel wholesalers of 15.81%. However, the court does not hint as to the appropriate standard; the court does not sit as a super-administrator to set the standards.

ministrator makes no provisions and takes no measures to offset the loss.[28] The Administrator further refused to comply with holding yearly reviews as to prices for a year in which that was a change in control of Suiza. No statutory allowance is provided for said exception. In fact a change of ownership amounted to an unwarranted de facto determination of an illegal act by mere change of control in ownership which is, of course, plainly in error under any corporate law standards. The change of ownership of Suiza prejudiced and punished Tres Monjitas, a separately owned milk processor company. Further in the order of 2007, the rules were substantively changed for the first time to consider as income of the two plants income derived from other non regulated business as is the case of the sale of juices. Up to said date by virtue of a final court order, unregulated business income was not to be counted, be it loss or profit. Again the court notes a change in the regulating parameters. The federal constitutional deficiency is not the open violation to a final court Commonwealth order but to the establishment of a new parameter without any prior notice to the plants and showing no nexus with the regulated dairy industry.[29] The court concludes that all parameters/criteria dis-

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[28] The court has strongly suggested that as to increases in fuel, electricity, certain raw materials, dairy supplements and foods for the agricultural herds, ORIL set forth a system of rapid/automatic increases/decreases be established though accelerated procedures similar to that established by the Consumer Affairs Department in the regulation of the cement industry in the early 1970's. This matter is, however, purely discretional but which may avoid further constitutional challenges on these grounds.

[29] This is yet another parameter-altered change providing the impression that a net result is originally sought and later the parameters are added/substracted to justify the net result.

cussed in this paragraph taken as a whole are deemed "arbitrary" in violation of due process.[231]

Finally and most critical the court tackles the thorny issue of Indulac being regulated exclusively to receive a price which is currently less than one half of the price of the cost of the dairy farmers. The price is financed by the fresh milk processors who pay more than the price deemed reasonable by the Administrator. The cost plus fair return rate of the dairy farmers was last established at 55cents per quart of milk. The actual price of a quart of milk paid by Indulac is 26-1/2 cents as calculated by Suiza.[232] Further, the cost of 26-1/2 per quart for purchase by Indulac as compared to around 65 cents per quart being paid by Suiza (counting the credit granted to Suiza to purchase raw milk for powdered milk produc-

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[231] The court is aware that the Legislature has placed the Administrator of ORIL in a difficult, potentially conflicting situation of wearing two hats. On the one hand he regulates the industry including the price scheme favoring the purchase of un-expensive raw milk by Indulac. On the other hand the Administrator sits in the Board of Directors of Indulac, a regulated party. A chamber of horrors factual scenario can very well occur. On the one hand the Administrator establishes one day a price for raw milk for Indulac to be purchased from the dairy farmers and within the next few days he sits as a Board of Director to approve Indulac's action, as they have done, to unilaterally increase the price paid by Indulac to the dairy farmers although said unilateral conduct may be against the law. P.R. Laws Ann. Tit. 5 § 1111 (Unfair business practices; disrruption of the market — prohibiting in the regulated market undermining the prices set of raw milk by the Administrator; prohibiting in the regulated marked reduction in prices in any distribution medium.

[232] Even if the price is only 32 cents without taking into account the recent reduction of April 5, 2007 for raw milk used for cheese, powdered milk, evaporated milk production was allowed to be purchased at 20 cents and 12 cents for the last two productions, the final below cost payment is substantial.

tion), the difference in price is substantial and prima facie discriminatory if considered that Indulac is now a strong competitor in the market and is no longer a mere "balancing plant" to purchase the surplus milk not used by the fresh milk processors. The current regulation requires the milk produced within quota to be purchased by Indulac. Fresh milk processors pay at .66125 (except powdered milk); Indulac pays 0.32 except for raw milk purchased for the production of cheese, evaporated milk and powdered milk (totaling 0.26 -1/2 for all purchases of raw milk). The milk processors purchase most of the milk; Indulac purchase the excess.[253]

Armed with a low cost of raw milk Indulac has increased their share of the general milk market from 38.40 million quarts in 1998 to 69.93 million quarts (increase of 82%) (Ex. 29) and on the other hand the fresh milk market has declined from 318.50 million quarts in 1998 to 275.27 million quarts in 2004 (Ex. 28-30) (14% decrease). Further and most critical the dairy farmers in control of both the FFIL and Indulac have expressed, even throughout the period of the injunctive hearing, a desire to purchase the two fresh milk industrial plants. The court notes the obvious, the lower the market sales of the fresh milk plants and the higher the market of Indulac, controlled by the dairy farmers, the lower the

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[253] As a result in the continued loss of the FFIL Capital fund discussed supra at the Findings of Fact section of this Opinion and Order the over quota milk produced by the dairy farmers is no longer liquidated at 100% of the quota. Recently the first 5% of the quota assigned is also not liquidated. Order of Jan. 3, 2006 (Docket No. 446, Order at Addendum #10). Further, FFIL now liquidates pursuant to recent order of June 13, 2007 as follows — 5% within quota not liquidated; thereafter 10% within quota liquidated at 30 cents; 20% within quota liquidated at 50 cents; 70% within quota liquidated at 70 cents. See Order at Docket No. 474, Addendum #3).

economic value of the two plants enabling a cheaper price for the purchase. Further the gains in the market of Indulac are undoubtedly caused at least partially by the purchase of raw milk at extremely low prices.

However, the court finds that the elimination of the fresh milk processors is contraindicated by various sections of the law of the enabling law. The court explains.

Article § 16 of Act 34 known as The Milk Industry Act of June 11 of 1957 codified at P.R. Laws Ann. Tit. 5 § 1092 particularly at § 1107(b) states the following:

> (B) In determining the limit of the regulation of the industry, the Administrator shall take into account the needs and interests of the different sectors within the industry so that any measure adopted will tend to stabilize and stimulate the progress in the production and marketing of milk and its byproducts and therefore further the prosperity of the industry.

This particular section emphasizes that the regulation of the industry is geared to "stabilize and stimulate the progress and marketing of milk and its by products" and "therefore further the **prosperity of the industry**" as opposed to one section of the industry or one particular party of the industry.

Further, at Subsection (e) the law mandates the following:

> . . . He shall, likewise, make thorough economic studies, at least every four (4) years, for the purpose of revising and keeping the price of fresh milk within a reasonable and equitable margin for the different sectors

> within the industry, that is, producers, processors, distributors of the product and consumers in general.

This section in particular requires that every four years a thorough economic study be made by the Administrator of the "fresh milk" to provide a "reasonable and equitable margin for **the different sectors within the industry** that is the producers (dairy farmers); processors (fresh milk as well as UHT processors); distributors . . . and consumers . . ." The court notes that the protected market is fresh milk considering equitable margins to all within the industry including the dairy farmers and the processors.

The court finds nowhere within the law a purpose of eliminating the milk processors through purchase of the dairy farmer or of creating an absolute control of the entire industry by the dairy farmers. To the contrary the protection offered by the mandate of the law is to all the industry as opposed to a particular section.

Further, Legislative History and Declaration of Purposes of the law narrates the purposes of the law.

> "To regulate the dairy industry and provide for the creation of a Fund for its development; to create the Office of the Administrator of the Regulation of the Dairy Industry, determine its power and to empower it to regulate said industry; to create a Consultive Board; to establish penalties for violations to this law; to derogate Law No. 106 of June 28, 1956 and to validate the official actions pursuant to said statute and for other purposes.

## LEGISLATIVE HISTORY AND DECLARATION OF PURPOSES

In the middle of last year, the Special Committee created by Resolution Number 77 of the Senate conducted a study on the production, manufacture and distribution of milk in Puerto Rico. The study revealed that the dairy industry was in crisis: a chaotic situation affected the consumers, producers and manufacturers of milk due to the deficient commercial relations that existed among the manufacturers themselves and between them and the producers.

The detailed investigation performed and the testimonies rendered by the persons who attended the public hearings held by the Special Senate Committee served as a reasonable basis to reach conclusions to the effect that: there existed a chaotic situation in the dairy industry due to the interests in conflict among the manufacturers themselves and between them and the producers, the efforts of the producers and the manufacturers to resolve the chaos had been unsuccessful because they had not been able to reach an agreement, if said situation continued a collapse would occur in this important industry in detriment to the health and economy of the country, the factory for the manufacture of surplus established by the manufacturers and products had not been able to function well due

to the conflict between the producers and the manufacturers, there had been an enormous amount of milk destroyed at said factory for which there is a potential market in Puerto Rico since the average consumption of milk in the country is less than 50 percent of what is advisable, and despite the increase registered in the production of milk and of the surplus that was wasted, the consumer price remains static or tends to increase.

All of the interested parties that concurred to the hearings held by the Special Senatorial Committee — producers, manufacturers and consumers — requested that the Government create an organism that would regulate the relations between the parties in order to establish the definite basis for the development and the stability of the dairy industry, and to seek a way to better distribute and market the main product and its by-products.

In view of this evidence presented at the public hearings referred to above, the report of the Special Senatorial Committee recommended the creation of a regulatory body for the dairy industry and that it be given powers, among others, to: (1) instrument regulations that will allow to dispose of the milk surplus in such a manner that, without affecting the interests of the persons engaged in operating businesses in the different phases of the industry, the

consumer would be provided dairy products that will gradually substitute imported products, (2) organize educational campaigns geared to increasing the consumption of fresh milk, (3) organize the elaboration, distribution and marketing of fresh milk, instrumenting a better distribution that will consider the best methods to reduce costs.

In attention to the recommendations of the Special Senatorial Committee, and due to the grave crisis that exists in the dairy industry, the Office of the Administrator of the Regulation of the Dairy Industry was created. This organism was granted ample power to create regulations to adequately resolve the chaotic situation which the dairy industry was experiencing.

The Legislative Assembly through this law clarifies and ratifies its original intention with regard to the regulation of the dairy industry. In this manner the Legislative Assembly wishes to emphasize its intention that the State, in the exercise of its police power and for the purpose of promoting the general welfare, intervene directly with the dairy industry, so that through adequate regulations it will be able to straighten its course so that the public interest will be adequately served through the greatest production of milk and pure dairy products by a vigorous, sound and progressive industry that oper-

> ates efficiently and that can offer milk and dairy products to the consumer at fair and reasonable prices.

It is evident that the disagreements of today existed fifty years ago in 1957 between dairy farmers and fresh milk processors[234]; a collapse of the milk industry was very near; the problem of excess milk and the disposal thereof was one of the disagreements between dairy farmers and fresh milk processors (as it is today). All agreed that principal commodity to be protected was the fresh milk and all further agreed that the solution to the problem was to develop a method to handle excess milk "without affecting the interest of the persons engaged in guiding business." The solution contemplated was not to hurt any of the entities within the milk industry. Obviously, the solution is not hurting a party by a regulation wherein the price of milk is lowered for one of the competitor, to the point of being purchased by a competitor, or by one of the members of the industry, as is occurring in the instant case. Further, the elimination of one of the key players of the industry purchased by another or a de facto monopoly of the industry to one of the parties within the industry was not contemplated and in fact was contraindicated by the express language of "without affecting the interest" to the entities at "engaged in operating the business." The different price

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[234] The Supreme Court of the United States has recognized the control of local dairy industry by dairy farmers and the potential clashes with the milk processors, together with the "political effectiveness of the local dairy farmers." See *West Lynn Creamery v. Healy*, 512 U.S. 186, 114 S. Ct. 2205, 129 L. Ed. 2d 157 (1994) N. 22, citing G. Miller "The Industrial organization of Political Production," 149 Journal of Institutional and Theoretic Economics 769 (1993)."

scheme favoring one of the parties is discriminatory, against public policy and hence irrational.

The court must, therefore, conclude that the elimination of one of the components of the industry is "demonstrably irrelevant to the policy the Legislature is free to adopt." *Tenoco Oil Co.*, 876 F.2d at 1024. Hence, the court must strike the policy of establishing the discriminatory practice of purchasing raw milk by Indulac at below cost numbers of the dairy farmers as compared to over cost payment by the milk processors. Said practice is prohibited by this court in any subsequent order of the Administrator of ORIL.

The current milk pricing scheme, however, has contributed to a continuous decrease in the demand for fresh milk and in the economic resources available to satisfy the demands of the milk industry. The alarming increase in the liquidation deficits and the FFIL's inability of payment in the last liquidations clearly show that there is not enough money available to pay the dairy farmers, hence, a clear proof of a decadent market. In sum, as the demand for fresh milk decreases, the larger the amount of surplus milk, which translates in less money available for compensation to the daily farmer. Thus, the Court is forced to conclude that the milk pricing scheme is not sustainable, as the nexus between the government's legitimate interest and the rationality of the regulation to pursue this interest is lacking.

***The Takings Clause***

The First Circuit, as well as other circuits, have clearly established that an economic regulation may be irrational enough in its enforcement, as to violate the Due Process and Equal Protection Clauses, also resulting in violation of the Takings Clause. *Tenoco Oil Co.*,

876 F.2d at 1026-1027. "A price regulation which forces wholesalers to sell gasoline for a price which does not cover operating costs and a reasonable profit may, in short order, become so onerous that the wholesalers will be unable ever to recover their earlier cumulative losses through subsequent price increases and may be forced out of business." *Id.*

In *Duquesne Light Company v. Barasch*, 488 U.S. 299, 307, 109 S. Ct. 609, 102 L. Ed. 2d 646 (1989), the Court held:

> The guiding principle has been that the Constitution protects [regulated businesses] from being limited to a charge for their property serving the public which is so "unjust" as to be confiscatory. *Covington & Lexington Turnpike Road Co. v. Sandford*, 164 U.S. 578, 597, 17 S. Ct. 198, 41 L. Ed. 560 (1896) (A rate is too low if it is "so unjust as to destroy the value of [the] property for all the purposes for which it was acquired," and in so doing "practically deprive[s] the owner of property without due process of law"); *Federal Power Commission v. Natural Gas Pipeline Co. Of America*, 315 U.S. 575, 585, 62 S. Ct. 736, 86 L. Ed. 1037 (1942) ("By long standing usage in the field of rate regulation, the 'lowest reasonable rate' is one which is not confiscatory in the constitutional sense"); *Federal Power Commission v. Texaco Inc.*, 417 U.S. 380, 391-392, 94 S. Ct. 2315, 41 L. Ed. 2d 141 (1974) ("All that is protected against, in a constitutional sense, is that the rates fixed by the Commission be high-

> er than a confiscatory level"). **If the rate does not afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments. As has been observed, however, "[h]ow such compensation may be ascertained, and what are the necessary elements in such an inquiry, will always be an embarrassing question."** *Smyth v. Ames*, 169 U.S. 466, 546, 18 S. Ct. 418, 42 L. Ed. 819 (1898). *See also Permian Basin Area Rate Cases*, 390 U.S. at 790 ("[N]either law nor economics has yet devised generally accepted standards for the evaluation of rate-making orders"). (Emphasis ours).

The analysis of whether confiscation or a taking of property in a regulated market has actually occurred cannot be done in a vacuum. After all, ". . . the impact of certain rates can only be evaluated in the context of the system under which they are imposed." Id. In this context, the court "must examine the manner in which the [agency] has employed the methods of regulation which it has itself selected. . . " *Permian Basin*, 390 U.S. 747, 792, 88 S. Ct. 1344, 20 L. Ed. 2d 312 (1968).

ORIL has lacked stability in the use of regulatory standards for the determination of allowable costs and reasonable prices, which provides the Administrator unlimited discretion to arbitrarily allow and disallow costs and change the rules applicable to operating and costs' expenses at will, in order to keep milk prices low, while forcing the fresh milk processors to pay the excessively high price for raw milk to subsidize Indulac. ORIL's "de-

cision to arbitrarily switch back and forth between methodologies" to achieve that result raises "serious constitutional questions." *Duquesne*, 488 U.S. at 315. The lack of regulatory rules has been the instrument through which plaintiffs have been denied the recovery of their costs, as well as a "fair profit" in their fresh milk business.[235]

In a pricing scheme, the expenses may be disallowed provided that an abuse of discretion on the part of the regulated corporation is established. *State of Missouri ex rel. Southwestern Bell Telephone Co. v. Public Service*

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[235] There is really no comparison between the situation of plaintiffs here and that of plaintiffs in *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 109 S. Ct. 609, 102 L. Ed. 2d 646 (1989). In the first place, the regulatory activity in *Duquesne* was supported by clear regulatory parameters. Secondly, plaintiff in *Duquesne* was protesting the regulatory body's refusal in allowing it to recover the investment costs (capital expenses) associated with the construction of plants that later on turned to be unnecessary. But plaintiffs in *Duquesne* were not trying to recover legitimate operating expenses but investment expenses that were never intended for public use. The Supreme Court, however, refused to intervene because plaintiffs admitted that they were recovering a reasonable return on investment even without recovering this particular investment cost. In this case we have concluded, that plaintiffs are not recovering even their operational costs because of the arbitrary way in which ORIL has manipulated the numbers for regulatory purposes. Needless to say, much less are plaintiffs recovering a reasonable rate of return on the capital investment, as has been discussed in this opinion and order. Lastly, in *Duquesne* no argument has been made that the regulated "rates jeopardize the financial integrity of the companies, even by leaving them insufficient operating capital or by impeding their ability to raise future capital. Nor has it been demonstrated that these rates are inadequate to compensate current equity holders for the risk associated with their investments under a modified prudent investment scheme." *Duquesne* at 312. The opposite, however, constitutes the facts in the instant case.

*Commission of Missouri*, 262 U.S. 276, 289, 43 S. Ct. 544, 67 L. Ed. 981 (1923). A presumption of correctness favors the books of a public service corporation. *West Ohio Gas Company v. Public Utility Commission of Ohio (#1)*, 294 U.S. 63, 68, 55 S. Ct. 316, 79 L. Ed. 761 (1935). Thus, the expenses are presumed to be incurred in good faith. *West Ohio Gas Company*, 294 U.S. at 72; *State of Missouri*, 262 U.S. at 288-289. These legal principals are particularly applicable to the instant case, as to the cost of plastic containers; professional and expert fees necessary for annual review; discounts to agents and promotions; shrinkage factors; returned milk, and other criteria not well handled by ORIL as previously discussed herein.

The Court finds that ORIL has failed to follow these principles and has intentionally squeezed plaintiffs between the cap of a fixed regulated price and an irrational high price for raw milk. ORIL has intentionally issued this administrative measure in order to protect Indulac in the competition with the local fresh milk industry and the continental importers. The evidence shows, from admissions of the farmers, that ORIL's price fixing scheme is designed to fulfill these goals. Based upon the expense statistics for the year 2003, and even before adjusting the same downwards, ORIL was acting in a regulatory defective way. ORIL should have used the actual 2004 expense statistics that it had. *W. Ohio Gas v. Public Utility Commission of Ohio (#2)*, 294 U.S. 79, 82, 55 S. Ct. 324, 79 L. Ed. 773 (1935). Moreover, ORIL had enough evidence available to support an advanced forecast on the impact that the expenses' increase will have on the fresh milk processors for the year in which the rates were to be in place, that is, in April 2005 and forward.

The taking of property may also be triggered by ORIL's lack of announced known regulatory standards, which allows ORIL to switch back and forth freely on the methodology used to make different adjustments at will so as to bring the cost of the milk processors down. ORIL's practice raises serious constitutional questions. *Duquesne*, 488 U.S. at 315. In *Duquesne*, *supra*, a case similar to the case at bar, when the volume of milk produced was excessively high, a "decision to arbitrarily switch back and forth between methodologies" for an income adjustment was discretionary allowed in order to make the necessary adjustments on the return of capital and investments calculations, professional fees, and transfer of prices, provided that these adjustments were made within the scope of the abuse of discretion rule cited therein. *Id.* Hence, in the instant case, ORIL has acted improperly by eliminating the processors' costs for experts' fees and professional fees that were related to the pricing rate scheme or as part of operational costs. *Driscoll v. Edison Light and Power Company*, 307 U.S. 104, 120-121, 59 S. Ct. 715, 83 L. Ed. 1134 (1939).

Plaintiffs further argue that they are convinced that ORIL is not willing to objectively address plaintiffs' financial costs and/or fair rate of return or investment within the milk pricing scheme simply because these needs are contrary and incompatible with the economic interests of Indulac, the dairy farmers, causing a fictitious need to maintain the cost of the milk to the consumer low. The Court does not quarrel with the Government's laudable interest to maintain the price of milk low to the consumer. The problem is in the methodology used to set the price, the cost of production and cost of operations, and lack of adequate standards in that they are constantly in a flux, sometimes recognized other times banned. Above all the fair rate of return is based

on a stale national average figure dating back to 1997, which is outdated when it is used for the years 2003 to 2007, particularly after May 2006, the date when the Puerto Rican Bonds were devaluated by Moodys. The Court is mindful that Indulac was created by the government to develop a side market within the milk industry by producing milk related products derived from milk that otherwise would have been discarded, and to protect the dairy farmers from suffering a production loss.

It is plaintiffs' contention that ORIL's announcing its intention of adopting an automatic price revision rule to take into account certain major increases in expenses, means very little. Any automatic adjustment formula must begin with a rational price level to be fairly established according to preexisting and pre-announced regulatory parameters. Since Puerto Rico has never determined prices in a scientific non-arbitrary way, an automatic price adjustment formula makes little sense until an initial scientific price determination is adopted.

The most glaring example of a taking is the establishment of a fair return rate or investment. The same is based on a stale average of rate of return in the continental United States published in 1997. But there is no scientific method used as to how Puerto Rico "fits" within the average. The average in the United States was published in 1997 but applied in Puerto Rico in 2003 through 2007, in stale fashion against the guidance provided in *Tenoco Oil*, 876 F.2d at 1024 (stating that a price regulation is stale if the figures are not current — five years deemed stale). Further, the rate of return does not take into consideration critical economic facts that occurred in Puerto Rico in May 2006, such as the devaluation of Puerto Rico bonds by the evaluation of Moodys.

Further, the regulatory scheme fails in that there is no procedure allowing for regulatory accrual of losses which occur from one yearly review to the next. The losses that occur from one year to the subsequent year are not accrued allowing for the losses incurred in a regulated market to be recuperated.

In sum, the current milk price scheme clearly represents a taking of property for the milk processors by not allowing them to recover their true costs and the allowance of a fair profit. The current situation of the milk price scheme is responsible for the dire financial situation of plaintiffs today.

**B. The Dormant Commerce Clause.**

Article I, Section 8, Cl. 3 of the United States Constitution confers upon Congress the affirmative power "to regulate commerce . . . among the several States." This affirmative power to regulate includes "a negative aspect, known as the dormant Commerce Clause" *Grant's Dairy—Maine, LLC v. Commissioner of Maine Department of Agriculture, Food & Rural Resources*, 232 F.3d 8, 18 (1st Cir. 2000). As summarized by First Circuit in *Pharmaceutical Research and Manufacturers of America v. Concannon*, 249 F.3d 66, 79 (1st Cir. 2001):

> The constitutional provision affirmatively granting Congress the authority to legislate in the area of interstate commerce "has long been understood, as well, to provide 'protection from state legislation inimical to the national commerce [even] where Congress has not acted. . . '" *National Foreign Trade Counsel v. Natsios*, 181 F.3d 38, 61 (1st Cir. 1999) (alterations in original) (quoting *Barclays Bank PLC v.*

> *Franchise Task Board of California*, 512 U.S. 298, 310, 114 S. Ct. 2268, 129 L. Ed. 2d 244 (1994)), aff'd *sub nom. Crosby v. National Foreign Trade Council*, 530 U.S. 363, 120 S. Ct. 2288, 147 L. Ed. 2d 352 (2000). This negative command known as the dormant Commerce Clause, prohibits states from acting in a manner that burdens the flow of interstate commerce. *Oklahoma Task Commission v. Jefferson Lines, Inc.*, 514 U.S. 175, 179-180, 115 S. Ct. 1331, 131 L. Ed. 2d 261 (1995); *Healy v. Beer Institute*, 491 U.S. 324, 326 n.1, 109 S. Ct. 2491, 105 L. Ed. 2d 275 (1989).

The purpose of the Dormant Commerce Clause doctrine is to prohibit "protectionist state regulation designed to benefit in-state economic interests." *Grant's Dairy*, 232 F. 3d at 18 (citing *Fulton Corporation v. Faulkner*, 516 U.S. 325, 330, 116 S. Ct. 848, 133 L. Ed. 2d 796 (1996) and *New Energy Company v. Limbach*, 486 U.S. 269, 273-274, 108 S. Ct. 1803, 100 L. Ed. 2d 302 (1988)).

Following the mandate of the Supreme Court in *West Lynn Creamery v. Healy*, 512 U.S. 186, 114 S. Ct. 2205, 129 L. Ed. 2d 157 (1994), the First Circuit has indicated that the application of the Dormant Commerce Clause doctrine requires a "sensitive, case-by-case analysis of purposes and effects" Id. at 201; *Grant's Dairy*, 232 F. 3d at 18-19; *Walgreen Co.v. Rullán*, 405 F. 3d 50, 55 (1st Cir. 2005).

Official state action can be discriminatory against interstate commerce in three different ways, to wit, (a) facially, (b) purposefully, or (c) in practical effect. *Wyom-*

*ing v. Oklahoma*, 502 U.S. 437, 454-55, 112 S. Ct. 789, 117 L. Ed. 2d 1 (1992). A facial discrimination against interstate commerce almost always results in a constitutional infirmity, that is *per se* invalid. *Fulton Corp. v. Faulkner*, 516 U.S. 325, 116 S. Ct. 848, 133 L. Ed. 2d 796 (1996) ("State laws discriminating against interstate commerce on their face are 'virtually *per se* invalid.'") (quoting *Oregon Waste Systems, Inc. v. Department of Environmental Quality of State of Oregon*, 511 U.S. 93, 114 S. Ct. 1345, 128 L. Ed. 2d 13 (1994)). Discriminatory effect results in a balancing approach with strict scrutiny for the state's justification. Since this is a constitutional attack on the application of regulatory power, the Court concentrates on the last two forms of discrimination under the analytical formulation of the First Circuit in *Walgreen Co.*, 405 F. 3d at 55:

> Under the dormant Commerce Clause, if a state law has either the purpose or effect of significantly favoring in--state commercial interests, over out-of-state interests, the law will "routinely" be invalidated "unless discrimination is demonstrably justified by a valid factor unrelated to economic protectionism" (citing *Houlton Citizens' Coalition v. Town of Houlton*, 175 F. 3d 178, 184 (1st Cir. 1999) which in turn quoted *West Lynn Creamery*, 512 U.S. at 192-193.)

As the Supreme Court itself has indicated, the legitimate purpose justifying the local discriminatory action has to be one that "cannot be served by reasonable nondiscriminatory alternatives." *Oregon Waste Systems, Inc. v. Department of Environmental Quality*, 511 U.S. 93, 101, 114 S. Ct. 1345, 128 L. Ed. 2d 13 (1994) (citing

*New Energy Co. of Indiana v. Limbach*, 486 U.S. 269, 278, 108 S. Ct. 1803, 100 L. Ed. 2d 302 (1988)). *See Walgreen Co.*, 405 F.3d at 59 (citing *Hunt v. Washington State Apple Advertising Com'n*, 432 U.S. 333, 353, 97 S. Ct. 2434, 53 L. Ed. 2d 383 (1977)). Justifications for "discriminatory restrictions on commerce must pass the 'strictest scrutiny'". *Oregon Waste Systems, Inc.*, 511 U.S. at 101 (citing *Hughes v. Oklahoma*, 441 U.S. 322, 327, 99 S. Ct. 1727, 60 L. Ed. 2d 250 (1979)). This balancing approach is called the Pike Test. *Pike v. Bruce Church, Inc.* 397 U.S. 137, 90 S. Ct. 844, 25 L. Ed. 2d 174 (1970). Rotunda and Nowack have stated:

> In these decisions one factor becomes imperative to the judicial tribunal, a legitimate state regulation must not burden interstate commerce in *either purpose or effect* unless the extent of that burden is outweighed by a legitimate state objective that cannot be achieved in a less burdensome manner. Rotunda and Nowak *Treatise on Constitutional Law*, Thompson-West (2007) s. 11.6 p. 199. (Emphasis added).

The Dormant Commerce Clause doctrine applies to Puerto Rico on the same terms that it applies to the states. *Trailer Marine Transport Corp. v. Rivera Vázquez*, et al., 977 F.2d 1, 8-9 (1st Cir. 1992). As to the applicability of the Commerce Clause to Puerto Rico, the Court of Appeals held:

> Both the Supreme Court and this court [First Circuit] have long held or assumed that Congress has power under the Commerce Clause to regulate commerce with

Puerto Rico. *See Secretary of Agriculture v. Central Refining Co.*, 338 U.S. 604, 616, 70 S.Ct. 403, 409, 94 L.Ed. 381 (1950) (Sugar Act of 1948 applied to Puerto Rico through the Commerce Clause); *Puerto Rico Tel. Co. v. F.C.C.*, 553 F.2d 694, 701 (1st Cir. 1977) (Federal Communications Commission regulations applied via the Commerce Clause to government-owned telephone company in Puerto Rico). Thus, in one aspect, the question "whether the Commerce Clause applies to Puerto Rico" has been settled in the affirmative for many years; the more precise issue posed in this case, is whether the dormant Commerce Clause doctrine also applies to Puerto Rico.

The Supreme Court has resolved this silence by holding that the power granted Congress under the Commerce Clause is not invariably exclusive of the states but only sometimes so. *Cooley v. Board of Wardens*, 53 U.S. (12 How.) 299, 13 L.Ed. 996 (1852). Pertinently, the Court's decisions hold, in an application that is opaquely called the dormant Commerce Clause, that state laws or local regulations are invalid under the Commerce Clause *ex propio vigore* where they unduly burden or discriminate against interstate or foreign commerce. *City of Philadelphia v. New Jersey*, 437 U.S. 617, 623-24, 98 S.Ct. 2531, 57 L.Ed.2d 475 (1978).

**The central rationale of the dormant Commerce Clause doctrine, as the Supreme Court has explained, is the dominant purpose of the Commerce Clause to foster economic integration and prevent local interference with the flow of the nation's commerce.** *H.P. Hood & Sons, Inc. v. Du Mond*, 336 U.S. 525, 537-38, 69 S.Ct. 657, 664-65, 93 L.Ed. 865 (1949). **This rationale applies with equal force to official actions of Puerto Rico. Full economic integration is as important to Puerto Rico as to any state in the Union. In a different context, the Supreme Court has flatly rejected the notion that Puerto Rico may erect an "intermediate boundary"separating it from the rest of the country.** *Torres v. Com. of Puerto Rico*, 442 U.S. 465, 472, 99 S.Ct. 2425, 2430, 61 L.Ed.2d 1 (1979). **There is no reason to believe that Congress intended to authorize Puerto Rico to restrict or discriminate against cross-border trade and ample reason to believe otherwise.** *E.g.*, 48 U.S.C. § 738 (no duties may be imposed on trade between Puerto Rico and the United States); 48 U.S.C. § 741a (Puerto Rico can tax imported goods but cannot discriminate in favor of goods made in Puerto Rico).

If the government of Puerto Rico were nothing other than the alter ego or immediate servant of the federal government, then the dormant Commerce Clause doc-

> trine would have no pertinence, for a doctrine designed to safeguard federal authority against usurpation has no role when the federal government itself is effectively the actor. (Citations omitted). Whatever the ultimate source of its authority or its exact constitutional status, Puerto Rico today certainly has sufficient actual autonomy to justify treating it as a public entity distinct from Congress and subject to the dormant Commerce Clause doctrine. In the Supreme Court's words, "the purpose of Congress in the 1950 and 1952 legislation was to accord to Puerto Rico the degree of autonomy and independence normally associated with States of the Union . . . . " *Examining Board v. Flores de Otero*, 426 U.S. 572, 594, 96 S.Ct. 2264, 49 L.Ed.2d 65 (1976). See also *Córdova & Simonpietri Ins. Co. v. Chase Manhattan Bank, N.A.*, 649 F.2d 36, 40-41 (1st Cir. 1981). (Emphasis added).

As to the First Circuit's prior holding in *Buscaglia v. Ballester*, 162 F.2d 805 (1st Cir. 1945), *cert. denied*, 332 U.S. 816, 68 S. Ct. 154, 92 L. Ed. 393 (1947), the appellate court overturned and succinctly stated "that *Buscaglia* will no longer be followed." *Trailer Marine*, 977 F.2d at 9. *See also Antilles Cement Corporation v. Acevedo Vila*, 408 F.3d 41, 46 (1st Cir. 2005) ("The dormant Commerce Clause and its doctrinal accouterments apply to Puerto Rico as though Puerto Rico were a state"); *Walgreen Co. v. Rullán*, 405 F.3d 50, 55 (1st Cir. 2005), *cert. denied*, 546 U.S. 1131, 126 S. Ct. 1059, 163 L. Ed. 2d 928 (2006) ("The dormant Commerce Clause doctrine, . . . applies to

Puerto Rico on the same terms as it applies to the states"); *United Egg Producers v. Department of Agriculture of the Com. of Puerto Rico, et al.*, 77 F.3d 567, 570-571 (1st Cir. 1996).

In a recent Puerto Rico Supreme Court opinion, *Asociación Puertorriqueña de Importadores de Cerveza, Inc. v. Estado Libre Asociado de Puerto Rico, et al.*, 171 P.R. Dec. 140, 2007 TSPR 92, 2007 Juris P.R. No. 98, 2007 WL 1630877 (2007), Justice Rebollo, in his concurring decision, cited *Trailer Marine, supra*, in support of his finding on the applicability of the Dormant Commerce Clause to Puerto Rico. Justice Rebollo explained that in *Trailer Marine*, the First Circuit made a thorough analysis on the applicability of the Dormant Commerce Clause to the then territory of Alaska and the United States Virgin Islands, citing *Anderson v. Mullaney*, 191 F.2d 123, 127, 13 Alaska 332 (9th Cir. 1951), and *JDS Realty Corp. v. Government of Virgin Islands*, 824 F.2d 256, 259-260 (3rd Cir. 1987):

> But we cannot conceive that in granting legislative power to the Territorial Legislature it **was intended that the power should exceed that possessed by the legislature of a State in dealing with commerce.** The words "all rightful subjects of legislation" describing the extent to which the legislative power of the Territory should extend, 48 U.S.C.A. § 77, do not include the imposition upon commerce such as that here involved of burdens which a State might not create under like circumstances. "All rightful subjects of legislation" must be held to refer to matters local to

> Alaska. *Anderson v. Mullaney*, 191 F.2d at 128. (Emphasis added).

*Asociación Puertorriqueña de Importadores de Cerveza, Inc.*, 2007 TSPR 92, 2007 Juris P.R. No. 98, 2007 WL 1630877. *See also United Egg Producers v. Department of Agriculture*, 77 F.3d 567 (1st Cir. 1996); *Starlight Sugar, Inc. v. Soto*, 253 F.3d 137 (1st Cir. 2001); *Walgreen Co. v. Rullán*, 405 F.3d 50 (1st Cir. 2005), *cert. denied*, 546 U.S. 1131, 126 S. Ct. 1059, 163 L. Ed. 2d 928 (2006).

Justice Rebollo further stressed that:

> There can surely be no doubt in anyone's mind that the United States — at least in trade commerce matters — enjoys broad powers to **prevent** what the United States Supreme Court has characterized as **"the tendencies toward economic Balkanization that had plagued relations among the Colonies and later among the States under the Articles of Confederation."** *Granholm v. Heald*, 544 U.S. 460, 472, 125 S. Ct. 1885, 161 L. Ed. 2d 796 (2005) (citing *Hughes v. Oklahoma*, 441 U.S. 322, 325-326, 99 S. Ct. 1727, 60 L. Ed. 2d 250 (1979)).

Most critical to Justice Rebollo was the express language provided in the Puerto Rican Federal Relations Act:

> Finally, in the absence of an express provision excluding Puerto Rico from the application of the dormant Commerce Clause, [n.13] there is no reason to believe that Congress authorized Puerto Rico to dis-

> criminate against interstate and foreign commerce. Likewise, it would be risky to argue otherwise, **given the existence of a prohibitive in the Federal Relations Act that orders the Legislature of the Commonwealth *"that no discrimination be made between the articles imported from the United States or foreign countries and similar articles produced or manufactured in Puerto Rico."*** Federal Relations Act sec. 3, L.P.R.A., vol. 1.

Moreover, Justice Rebollo found persuasive the analysis made by Constitutional law commentator Laurence H. Tribe:

> According to the distinguished commentator Laurence H. Tribe, the United States Supreme Court's approach to this matter lays great emphasis on the question whether the statute at issue discriminates against interstate or foreign [out-of-state] commerce. Tribe, *supra*, at 1059. Consequently, a state law that discriminates against interstate commerce, ***either on its face or in its practical effect***, will be invalidated unless the state shows that the statute serves a legitimate local purpose and that this purpose cannot be served as well by nondiscriminatory means. *Id.* (Emphasis added).

*Asociación Puertorriqueña de Importadores de Cerveza, Inc.*, 2007 TSPR 92, 2007 Juris P.R. No. 98, 2007 WL 1630877. *See also Ramos v. Puerto Rico Medical Ex-*

*amining Bd.*, 491 F. Supp. 2d 238, 2007 WL 1745654, *3, n.4 (D.Puerto Rico) (June 18, 2007):

> In order to resolve the present controversy it is unnecessary to determine whether the Privileges and Immunities Clause of the United States Constitution applies to Puerto Rico *ex propio vigore*. The court notes, however, that like the Commerce Clause, the Privileges and Immunities Clause derives from Art. IV of the Articles of the Confederation, and was intended to create a national economic union.

In the instant case, defendants challenge the standing of plaintiffs. The Court, however, finds that plaintiffs have *prima facie* standing to proceed with this Dormant Commerce Clause challenge. As stated above, plaintiffs are required to pay for the raw milk an amount much higher than the amount constituting the farmers' cost and reasonable profit in order for Indulac to be able to buy the same milk at a price way below that level, without affecting the dairy farmers' income. When Indulac turns this milk into fluid milk it directly competes with the fresh milk processors and affects their market share and their general competitiveness in the fluid milk market of Puerto Rico. The milk pricing scheme currently under attack exists only because most of the financial burden is carried by plaintiffs. Indeed, plaintiffs carry on with the recovery of expenses, reasonable profit of the dairy farmers, and the competitive weight of having their market share in the Puerto Rico fluid milk market eroded by Indulac's activities, their subsidized competitor. The market share has caused an adverse erosion in plaintiffs' financial condition. Contrary to defendants' position, it is clear that a plaintiff in dormant Commerce

Clause cases does not have to be a member of the class of entities against which the state measure discriminates. In *Houlton Citizens' Coalition v. Town of Houlton*, 175 F. 3d. 178, 183 (1st Cir. 1999), the Court said:

> In Commerce Clause jurisprudence, cognizable injury is not restricted to those members of the affected class against whom states or their political subdivisions ultimately discriminate. See *General Motors Corporation v. Tracy*, 519 U.S. 278, 286, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997). *Thus, an in-state-business which meets constitutional and prudential requirements due to the direct or indirect effect of a law purported to violate the dormant Commerce Clause has standing to challenge that law.* (Emphasis added).

In *Houlton*, 175 F.3d at 183, the Court set forth the normal prudential considerations of standing:

> Here, Faulkner, a co-plaintiff satisfies both the constitutional requirements and the prudential conditions for standing. He has lost the business of his residential customers in Houlton; that injury can be traced directly to the Town's neoteric waste management scheme; and the injury would be adequately redressed by equitable relief and/or damages against the Town. As a classic plaintiff asserting his own economic interests under the Commerce Clause (a constitutional provision specifically targeted to protect those interests) Faulkner **avoids any concerns relative either to**

> ***jus tertii***, *Warth v. Seldin*, 422 U.S. 490, 499, 95 S. Ct. 2197, 45 L. Ed. 2d 343 (1975), **or to the "zone of interest" requirement,** *see Valley Forge Christian College v. Americans United for Separation of Church and State, Inc.*, 454 U.S. 464, 475, 102 S. Ct. 752, 70 L. Ed. 2d 700 (1982). (Emphasis added).

Further, in *Alliance of Auto. Mfrs. v. Gwadosky*, 430 F. 3d 30 (1st Cir. 2005), the First Circuit again followed *Houlton*, and held that the state measure under attack discriminated against interstate commerce by favoring in-state automobile dealers at the expense of out-of-state automobile dealers. But the financial burden of the system that the state had in place was carried mainly by the Ford Motor Company and other automobile manufacturers. These entities were not competitors of the automobile dealers of either state, thus, not similarly situated amongst them. However, Ford paid the financial burden of the barrier that was erected against interstate commerce; therefore, the association to which Ford belonged was granted standing. *See also Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 104 S. Ct. 3049, 82 L. Ed. 2d 200 (1984); *General Motors Corp. v. Tracey*, 519 U.S. 278, 286, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997). In the instant case, plaintiffs have the financial burden of subsidizing Indulac, the dairy farmers, and ultimately, the responsibility of keeping the milk industry afloat, regardless of the cost. Hence, plaintiffs have standing to challenge the government's violation of the Dormant Commerce Clause.

The price discrimination regulation under scrutiny fails both the "purpose" and "effect" tests.[236] There is no dispute on the record on any of the two counts. The Administrator of ORIL, Juan Pedro Gonzalez, testified about the pricing of $0.32 per quart of surplus milk for Indulac contained in the provisional administrative order of February 24, 2006. Very eloquently, he explained the need for that discriminatory pricing in the following way:

> "If right now, instead of .32 cents we were to raise the price of surplus milk to .53, .55 cents, and we lower the price of fresh milk to .53 or .55 cents in order for Indulac to be able to have a profit and continue in operation, we are going to have to raise the price of UHT milk to 1.30 or 1.50 per liter or quart. And if we are going to do that today without these [protective] two bills of law, the imported UHT milk is going to take over the entire market and it will make Indulac go bankrupt." *See* Transcript of February 27, 2006, at pages 34-35.

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[236] When considering a possible Dormant Commerce Clause violation, the Court shall carefully examine the circumstances on a case-by-case basis. All "[f]ormulas for applying the dormant Commerce Clause are, if flexible enough to be valid, usually too general to resolve concrete cases. Still, the formulas offer a starting point and, under the precedents, state action that 'discriminates against interstate commerce'" stands condemned." *Trailer Marine Transport v. Rivera*, 977 F.2d 1, 10 (1st Cir. 1992). (citations omitted) *See also Walgreen v. Rullán*, 405 F. 3d at 55. Here, our purpose and effect analysis is firmly grounded in the specific facts proven on the record. *West Lynn Creamery*, 512 U.S. at 201. The Court's justification to apply the Dormant Commerce Clause to Puerto Rico is simply because Puerto Rico ". . . may not place itself in a position of economic isolation". *Baldwin v. G.A.F. Seelig*, 294 U.S. 511, 527, 55 S. Ct. 497, 79 L. Ed. 1032 (1935).

This statement of the Regulator is confirmed by the testimony of Mr. Benitez, a dairy farmer and President of Indulac, who indicated that Indulac could not pay more than 32 cents because "We would not be able to compete with imported UHT or it [Indulac] would sustain economic losses." Both experts for defendants admitted that the justification for this price discrimination was the competition faced by Indulac from the UHT milk importers. The record shows that as recent as the year 2006, Indulac was requesting to the Administrator further price reductions in order to compete with imported UHT milk, and they were successful as the price was further reduced by allowing milk used for products, such as cheese, evaporated milk, etc., and by reducing required payments to be made to the FFIL by Indulac.

In the instant case, the record amply supports a finding of a constitutional violation of the Dormant Commerce Clause, as the milk pricing scheme is invalid *per se*. The mere purpose to discriminate against interstate commerce is sufficient to trigger a constitutional challenge of the Dormant Commerce Clause:

> If a state law discriminates against interstate commerce because of its interstate nature, the state law should be held to be a *per se* violation of the dormant Commerce Clause. Because the purpose of the law is illegitimate, there is no need for the Court to engage in any balancing test: Rotunda and Nowak, *Treatise on Constitutional Law* Thompson-West 2007 S.11.8 p. 220.[237]

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[237] The Court is mindful of the fact that the Supreme Court has "also recognized that there is no clear line separating the category of state regulation that is virtually *per se* invalid under the Commerce

Indulac's price subsidy is also questionable under the balancing "effect" test. As admitted by Mr. Pedró himself, if no protectionist laws are enacted, and Indulac is forced to pay an amount equal to the farmer's cost and a reasonable profit, then the imported UHT milk taking would take over the market forcing Indulac into bankruptcy. Hence, Indulac's price benefit not only has the purpose of stopping or at least limiting the market share of imports but it is having the desired effect.[238]

Puerto Rico's situation is similar to other milk cases already entertained by the United States Supreme Court finding a violation to the Commerce Clause. Puerto Rico is trying to compensate, through a subsidy paid by plaintiffs, the natural cost advantage of out-of-state milk producers in order to protect the local milk market as well as the local dairy farmers. The Supreme Court has consistently struck down such type of measures despite any local ingenuity.

"Nice distinctions between direct and indirect burdens [are] irrelevant" when purpose and effect is to sup-

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Clause and the category subject to the *Pike v. Bruce Church* balancing approach. In either situation the critical consideration is the overall effect of the statute on both local and interstate activity." *Brown-Forman Distillers Corp. v. New York State Liquor Authority*, 476 US 573, 579, 106 S. Ct. 2080, 90 L. Ed. 2d 552 (1986). See also *Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 298 n. 12, 117 S. Ct. 811, 136 L. Ed. 2d 761 (1997) ("There is, however, no clear distinction between these two strands of analysis").

[238] The milk production cost in Puerto Rico is much higher than that in the Continental United States. Indulac presently holds about 70% of the UHT milk market in Puerto Rico, a fact that makes the challenged regulation discriminatory. In sum, Indulac has control of almost 3/4 of the UHT milk market in Puerto Rico, simply because it has no competition, as Indulac subsidized price for raw milk cannot be defeated by UHT milk importers.

press or mitigate interstate competition. (*Polar Ice Cream & Creamery Co. v. Andrews*, 375 U.S. 361, 374, 84 S. Ct. 378, 11 L. Ed. 2d 389 (1964) (citing *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 55 S. Ct. 497, 79 L. Ed. 1032 (1935)) because they have the same effect as an interstate tax or custom duty). *Oregon Waste Systems, Inc.*, 511 U.S. at 106 (1994) (". . . regulating interstate commerce in such a way so as to give those who handle domestic articles of commerce a cost advantage over their competitors handling similar items produced elsewhere, constitutes . . . protectionism"). Measures that neutralize the natural advantages possessed by lower cost out-of-state producers are routinely held unconstitutional. *See Baldwin*, 294 U.S. at 527 (elimination of milk regulation "designed to neutralize advantages belonging to the [out-of-state] place of origin"); *West Lynn Creamery*, 512 U.S. at 194 (milk market); *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 104 S. Ct. 3049, 82 L. Ed. 2d 200 (1984) (liquor); *Hunt*, 432 U.S. at 351 (statute invalidated because it had "the effect of stripping away from the Washington apple industry the competitive and economic advantages it has earned for itself"); and other cases of this kind cited in *West Lynn Creamery*, 512 U.S. at 194 (calling them "legion").

In *West Lynn Creamery*, 512 U.S. 186, 114 S. Ct. 2205, 129 L. Ed. 2d 157, the "avowed purpose" and "undisputed effect" of the measures therein under attack were to "enable higher cost Massachusetts dairy farmers to compete with lower cost dairy farmers of other states" and to allow "Massachusetts dairy farmers who produce at higher costs to sell at or below the price charged by lower cost out-of-state producers."

The situation in *West Lynn Creamery, supra*, is similar to the case at bar. In *West Lynn Creamery*, the State

of Massachusetts imposed a tax on all the raw milk sold by dealers (both in and out-of-state) to Massachusetts retailers, and distributed the tax proceeds to Massachusetts' dairy farmers only. In the instant case, the Puerto Rico government imposes a surcharge on fresh milk processors that allows Indulac to receive low priced raw milk to compete with imported UHT milk while at the same time maintaining an elevated price for all the raw milk produced by the Puerto Rico dairy farmers. Both the *West Lynn Creamery* tax and the Puerto Rico surcharge are designed to and have the effect of interfering with commerce while channeling money to the local dairy farmer. Cf. *Bacchus Imports, Ltd.*, *Id.* (same effect achieved by exempting certain local liquor from state tax).

The record is devoid of any suggestion that this discriminatory pricing scheme is supported by any legitimate state interest unrelated to protectionism, and that said interest cannot be achieved by lawful means. These measures do not pass judicial scrutiny. To argue that this is a measure needed by Puerto Rico's "struggling" milk industry, is not enough. *Bacchus*, 468 U.S. at 272 (". . . we perceive no principle of Commerce Clause jurisprudence supporting the distinction between thriving and struggling enterprises under these circumstances, and the state cites no authority for its proposed distinction"). ("[T]he propriety of economic protectionism may not be allowed to hinge upon the state's (or this Court's) characterization of the industry as either 'thriving' or 'struggling'"). *Id.* at 273. *See also West Lynn Creamery*, 512 U.S. at 205 (rejecting this same argument with respect to the alleged possible collapse of the milk industry in Massachusetts, and citing for the same proposition another milk case, *Baldwin*, 294 U.S. at 522-523.)

Defendants' discriminatory practice is not saveable with the argument that it simply promotes the local products and that it does not intent to discriminate against the foreign products. *Bacchus*, 468 U.S. at 273 (". . . it is irrelevant to the Commerce Clause inquiry that the motivation of the Legislature was the desire to aid the makers of the locally produced beverage rather than to harm out-of-state producers"). A desire to either increase the market share of local producers or simply mitigate the declined demand for their products does not pass muster either. *West Lynn Creamery*, 512 U.S. at 196, n.12 ("For Commerce Clause purposes, it does not matter whether the challenged regulation actually increases the market share of local producers or whether it merely mitigates a projected decline"). The fact that for years Indulac has produced by-products that did not make a profit is irrelevant to our analysis of the Dormant Commerce Clause challenge. Firstly, Indulac is today a significantly profitable entity that has generated much of its profits from the UHT milk business for several years. Secondly, "the dormant Commerce Clause is applicable to activities undertaken without the intention of earning a profit." *Camps Newfound/Owatonna, Inc. v. Town of Harrison, Me.*, 520 U.S. 564, 584-85, 117 S. Ct. 1590, 137 L. Ed. 2d 852 (1997) (citing *Edwards v. People of State of California*, 314 U.S. 160, 62 S. Ct. 164, 86 L. Ed. 119 (1941).

Finally, the fact that the discriminatory measure allows Indulac to favorably compete with out-of-state interests, such as the UHT milk importers, as well as intrastate interests, such as the fresh milk processors, makes no difference. *Walgreen Co.*, 405 F. 3d at 58. Courts have invalidated laws under the Commerce Clause because "they discriminate against out-of-state entities and some in-state entities in order to favor a

subset of in-state interests." Id. (citing *C & A Carbone v. Town of Clarkstown*, 511 U.S. 383, 394, 114 S. Ct. 1677, 128 L. Ed. 2d 399 (1994)).

It is immaterial whether the competition from Indulac's UHT milk is a main cause for the declining volume of fresh milk or simply one of the factors. Every witness testifying on the subject agreed that it was at least a factor. The degree at which fresh milk is affected by UHT milk competition has no bidding for this constitutional analysis. *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263, 269, 104 S. Ct. 3049, 82 L. Ed. 2d 200 (1984). In *Baldwin v. G. A. F. Seelig, Inc.*, 294 U.S. 511, 55 S. Ct. 497, 79 L. Ed. 1032 (1935), a unanimous Supreme Court rejected the notion that a direct-indirect burden distinction could be relayed upon by the state to defend otherwise non-competitive scheme. *Associated Industries of Missouri v. Lohman*, 511 U.S. 641, 650, 114 S. Ct. 1815, 128 L. Ed. 2d 639 (1994) ("Actual discrimination, whatever it is found is impermissible, and the magnitude and scope of the discrimination have no bearing on the determinative question whether discrimination has occurred"); *Maryland v. Louisiana*, 451 U.S. 725, 101 S. Ct. 2114, 68 L. Ed. 2d 576 (1981).

The Court must cease its analysis at this point having determined the applicability of the Dormant Commerce Clause, having further set forth sufficient facts showing a strong federal factual scenario as to a *prima facie* violation, and having determined standing. The Court stops as it finds that any potential remedy as to the Dormant Commerce Clause has already been provided under *Permian Basin Area Rate Cases*, 390 U.S. at 769-70. The Court stated that a regulation begins to take property without due process of law only if "arbitrary, discriminatory or *demonstrably irrelevant to the policy*

*the legislature is free to adopt.*" (Emphasis ours). Based on the highlighted above quote, the Court has already found unconstitutional the regulation granting Indulac the privilege of purchasing raw milk at below cost process of the dairy farmers based on the fact that Indulac is using said benefit to give a competitive edge over the fresh milk processors, and the farmers are also using said regulatory scheme to attempt to purchase the two processing plants at a bargain price. The net result under either alternative is that the fresh milk processors are eliminated from the market which is clearly contraindicated by the Statement of Motives set forth in Law No. 34. The Milk Industry Regulatory Act clearly indicates that when establishing a procedure "to dispose of the milk surplus" the matter would be handled "in such a manner that [would not] affect [ ] the interest of the persons engaged in [the] operating [of the] businesses in the different phases of the industry." Hence, no milk industry party would be affected by the procedure of "dispos[ing] of the milk surplus through a regulation." The Court found, therefore, that the milk processors are steadily losing their market through the regulatory procedure of granting Indulac the right to produce milk at below cost of the dairy farmers. The Court struck said remedy as unconstitutional, which is the only remedy that can be achieved through the Dormant Commerce Clause. Hence, the Court finds that said remedy is, at this point, academic and under justiciability standards the court refuses to continue any further analysis.

**INJUNCTIVE RELIEF REVISITED**

Injunctive relief under Fed. R. Civ. P. 65 requires that a party seeking injunctive relief comply with a quadripartite test. *New Comm Wireless Services, Inc. V. SprintCom, Inc.*, 287 F.3d at 8-9.

The first criteria to be complied is likelihood of success, the sine qua non requirement. *Weaver v. Henderson*, 984 F.2d at 12. Should said requirement not be present, "the remaining factors become matters of iddle curiosity." *Auburn News Co., Inc. v. Providence Journal Co.*, 659 F.2d at 277. The court finds, as more fully described infra, violations of Due Process, Equal Protection and the Takings Clause, a pattern of lack of standards, change in standards with unfettered discretion, use of stale figures, and lack of an appropriate standard as to fair rate of return in the regulations set by the regulator all pointing to a taking "pursuant" to *Duquesne Light Co.*, 488 U.S. at 307; *Tenoco Oil*, 876 F.2d at 1026-1027.

The second criteria constitutes the presence of non-speculative irreparable harm. *Narragansett Indian Tribe v. Guilbert*, 934 F.2d at 6-7. The court finds that said criteria has been reached since the two processing plants are losing market and have suffered for the periods from 2003 to 2007 a Due Process and Equal Protection violation reaching levels of a "taking." The record is abundant as to the continuous violations for said period, including a methodology deficiency in parameters and unlimited discretion of the Administrator in changing, adding, subtracting, from year to year, parameters. Further, there is no system for a regulatory accrual to recuperate interim losses that occur from year to year, yet a stale system to determine "fair rate of return" is in place. These deficiencies point to permanent loss in market and long-standing violations of constitutional rights for extensive protracted periods of time. The court opines this criteria to have surpassed the required threshold.

The third criteria requires the court to perform a balancing of equities under *Matos ex rel. Matos v. Clinton School Dist.*, 367 F.3d at 73. The court balances whether "the harm caused plaintiff without the injunction, in light of plaintiffs likelihood of success in the merits, outweighs the harm the injunction will cause defendants." *DeNovellis v. Shalala*, 135 F.3d at 77.

Plaintiff is merely requesting that the regulations promulgated provide a "fair rate of return" and that the parameters set not be arbitrary. Defendants potentially will suffer the loss of continuing with an unquestionable discriminatory price preference as to the purchase of raw milk, financed by plaintiff, which is being used at least partially to dwindle plaintiffs share of the fluid milk market. Further, the dairy farmers are using said loss of market in an attempt to purchase the good will and market of plaintiff at a low price, all caused or partially caused by the preferential price scheme whereby Indulac buys raw milk at more than half the cost of plaintiffs and under the cost of the dairy farmers. The matter is not close. The constitutional rights of plaintiff override, with its consequential permanent loss of market and potential fire sale of its plants, the rights of defendant to continue with a preferential purchase price of raw milk which is prima facie discriminatory and must be ceased.

*The effect on the public interest.* Without the injunctive relief, the plants are close to being sold at very low prices, an important independent element of the industry is about to be lost and the industry is then close to being monopolized by one party of the milk industry. The public interest has been clearly set by the law: The court concedes that the excess milk be properly attended by government regulation; however, by disposition of the law (Legislative History and Purposes of the "Milk In-

dustry Regulation Act") said regulative procedure is to be performed "without affecting the interest of the persons engaged in operating [the] business . . . of the industry."

Hence, the public interest lies in the granting of the injunctive relief.[239]

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[239] The defendants allege that the court should not issue an injunctive relief based on the doctrine of "clean hands" as Plaintiffs acted as Director of Indulac and hence participated in the decision of Indulac. The court is of the opinion that the doctrine should not apply. *Dr. José S. Belaval, Inv. v. Perez-Perdomo*, 488 F.3d 11 (1st Cir. 2007) (clean hands doctrine "only applies when claimant's misconduct is directly related to the merits of the controversy between the parties . . .") First, the court clarifies that plaintiffs' industrial fresh milk processors, ceased to be members of the Board of Indulac on September 2, 2003 (Ex. 7, Transcript February 15, 2005, pp. 134-135). Further, the court has issued injunctive relief based on arbitrary parameter determinations relating exclusively to ORIL's conduct in accepting or rejecting production and/or operational costs and/or using stale figures in determining manufacturing and operational costs and/or in changing from year to year the parameters and/or in the application of a 1997 United States stale average "fair rate of return" to the 2003 to 2007 fair rates of return as to the milk industry in Puerto Rico. The conduct which the court attributes to ORIL as violating Due Process, Equal Protection and the Takings Clause of the Federal Constitution in regulating the milk industry lacks any participation by the two plants.

The court sets forth various illustrative examples. The two plants did not participate at all in the following:

— ORIL's decision in 2005 to terminate the credit for bona fide returned milk credited to retailers or wholesalers which fictitiously increased the real capital income of the two plants (in the past returns were accepted by ORIL).

— The plaintiffs did not participate in the decision of the Administrator in using sales figures of the plants of 2003 as basis for regulating industry prices in 2005, 2006, 2007. The use of stale cost figures does not allow for obvious increases in cost and operations

such as electricity, fuel, resin and labor that have occurred since 2003 to 2007. Sales had decreased as, known by ORIL, and again the capital base of the two plants on past sales is fictitious since the sales of fresh milk have actually decreased from 2003 to 2007. *Tenoco Oil Co.*, 876 F.2d 1024 (criticizing use of stale figures of years past the actual year of the review.)

— ORIL used as "fair return rates of investments" as to the plants a 1997 United States average figure of 10% applied to the regulatory prices set in 2003, 2005, 2006, 2007, without a study as to how Puerto Rico "fit" into the national average. The United States average of 10% is further stale being used in 2003 to 2007. *Tenoco Oil Co.*, Id. (The use of stale rates of return from the Continental United States to Puerto Rico fuel industry not found reasonble.) Finally, as to the yearly review of the price regulation for 2007, ORIL failed to take into consideration the economic reality of the devaluation of Four Billion Dollars of governmental Bonds of Puerto Rico by Moody's in May of 2006.

— The two claimants had no participation in the change of parameters by ORIL of discounts to agents although in years immediately before discounts were granted by ORIL; further discounts being actually taken by Indulac in amounts of around $1.8 million dollars and the regulator did nothing to stop these discounts. No parameters as to discounts are present since one year they are accepted by ORIL without reasoning and the next year they are surprisingly rejected.

— The credit granted as to shrinkage (loss of raw milk due to temperature) was diminished by ORIL without any explanation. The "historical factor" alleged by ORIL was proved to be nonexistent.

— ORIL refused to grant credit for operational costs of professional fees and use of experts relating to the annual review hearing; a criteria accepted to be credited by the Supreme Court. *Driscoll v. Edison Light & Power Co.*, 307 U.S. 104, 59 S. Ct. 715, 83 L. Ed. 1134.

— There is no mechanism to recuperate losses occurring between yearly periods of price review. That is, there is no regulatory accrual for the losses that occur from year to year. Hence, the plants must carry the losses and never are able to recuperate losses.

## THE REMEDY

In view of the foregoing, plaintiffs' petition for preliminary injunctive relies if **GRANTED** as follows:

Effective immediately, both the fresh milk processors and Indulac will begin paying the amount of $0.55 per quart of raw milk to the dairy farmers. When the Administrator eventually determines to change the price to be paid to said dairy farmers, all market participants using raw milk to process fluid milk will pay the same amount for the milk. Under no circumstances will the fresh milk processors be required to pay more for their raw milk or carry additional costs for the purpose of allowing Indu-

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— In the 2007 review ORIL for the first time counted the revenue of the plants in non-regulated business (sale of non-regulated juice business) notwithstanding state court's final order to the contrary respected until 2007. The constitutional deficiency being again the changing of parameters.

— ORIL refused to hold a yearly increase regulatory hearing merely because of a change of ownership of Suiza; Tres Monjitas, a separately owned and managed company, suffered prejudice. The regulating statute contains no exception to the yearly reviews merely due to a change in ownership. A mere change in ownership fails to warrant a presumption of illegality under any corporate law analysis. Again the federal deficiency is a change in parameters.

— The current difference in prices of raw milk from the dairy farmers purchased by Indulac (around 26.5 cents) and that of the plaintiffs (around .65 cents) is a matter of legislation wherein the two plants have no determinative nor regulative capacity.

The court, therefore, considers that since the injunctive relief has been granted based on Due Process, Equal Protection and the Takings conduct attributed to ORIL where Suiza and Tres Monjitas are not involved in any "misconduct . . . directly related to the merits of the controversy between the parties" the doctrine of clean hands does not apply. *Texaco Puerto Rico, Inc. v. Department of Consumer Affairs*, 60 F.3d 867, 880 (1st Cir. 1995).

lac's access to raw milk for UHT or fluid milk manufacturing at a lower cost than the cost at which plaintiffs can acquire raw milk from fresh or fluid milk processing. The Administrator may set at his discretion the prices for raw milk for non fluid milk use.

In a period of no more than thirty (30) days, the Administrator will put into effect non-discriminatory, rational and scientific regulatory standards that will allow him to determine costs and fair profits return for all the participants in the Puerto Rico regulated milk market. Those standards will set the reasonable rate of return that each participant should receive. The Administrator shall perform a study as to the economic realities of doing business in Puerto Rico and the particular "fit" of Puerto Rico into any economic model which may be used from other jurisdictions. Any figures used from other jurisdictions are not to be stale but are to be "for the year in question." *Tenoco Oil Co.* The Administrator is to establish a system or incorporate a system or provide for mitigation for regulator accrual for losses properly supported that occur between periods of yearly reviews. The price structure of the fresh milk processors will be reviewed immediately under those parameters. The methodology of the parameters is to be consistent with this Opinion and Order.

The Administrator is ordered to adopt a temporary mechanism that will allow the processors to recover the new rate of return they are entitled to (whatever that may be) for the year 2003 (base cost year of the present structure) and up to the day when they begin to recover said rate based on the new regulatory standards and corresponding order. The Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of his choosing.

The period for this special recovery shall be reasonably determined by the Administrator. The Administrator will hold hearings for this purpose with the participation of plaintiffs, and all parties within the milk industry, within a period of thirty (30) days of this Opinion and Order. A decision by the Administrator shall follow promptly.

The court will retain jurisdiction until full compliance has been duly met with this preliminary injunction.

Upon compliance with the dispositions of this Opinion and Order, the parties shall forthwith move the court to schedule a hearing on the permanent injunction.

**IT IS SO ORDERED.**

## APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

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Civil No. 04-1840

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VAQUERIA TRES MONJITAS, INC., and
SUIZA DAIRY, INC.,
Plaintiffs,

*v.*

JOSE O. FABRE LABOY, in his official capacity as Secretary of Agriculture of the Commonwealth of Puerto Rico, and JUAN R. PEDRO-GORDIAN, in his official capacity as Administrator of the Milk Industry Regulatory Office of the Commonwealth of Puerto Rico,
Defendants.

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October 2, 2006

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## AMENDED OPINION AND ORDER

DOMINGUEZ, District Judge. The Court has determined to amend its Opinion and Order of September 30, 2006 (Docket No. 368) in order to clarify certain statements made by the Court. An *Amended Opinion and Order* is, thus, hereby issued.

Pending before the Court are several motions to dismiss, and Plaintiffs' opposition thereto: (a) *Motion To Dismiss First, Fourth And Fifth Causes Of Action Under Rule 12(b)(1) And Request For The Court To Refrain From Exercising Its Jurisdiction As To The Other Causes Of Action Pursuant To The Burford Abstention* filed by intervenor, Industria Lechera de Puerto Rico, Inc. ("Indulac") (Docket No. 225); (b) *Defendant José O. Fabré Laboy's Motion To Dismiss The Second Amended Complaint And Motion Requesting Abstention And That The Court Deny The Plaintiffs' Motion For Injunctive Relief* filed by the Hon. José O. Fabré Laboy ("Laboy") (Docket No. 227); (c) Plaintiffs' oppositions to the motions to dismiss (Docket entries No. 237, 238); (d) Indulac's reply to Plaintiffs' opposition (Docket No. 249); (e) Plaintiffs' sur-reply to Indulac's reply (Docket No. 257); (f) co-defendant José O. Fabré-Laboy's motion joining Indulac's reply (Docket No. 258); (g) *PRDFA's Motion Restating Motion To Dismiss As To Second Amended Complaint* filed by intervenor, the Puerto Rico Dairy Farmers Association ("PRDFA") (Docket No. 228); and (h) Plaintiff's opposition to PRDFA's motion (Docket No. 239). For the reasons set forth below, the motions to dismiss are **GRANTED IN PART AND DENIED IN PART.**

**Factual and Procedural Background**

On September 14, 2005, plaintiffs filed a Second Amended Complaint against the defendants, the Hon. José O. Fabré Laboy, in his official capacity as Secretary of Agriculture of the Commonwealth of Puerto Rico (the "Secretary"), and Mr. Juan R. Pedro-Gordian, in his official capacity as the Administrator of the Puerto Rico Milk Industry Regulatory Office (the "Administrator") (Docket No. 206). Plaintiffs seek a preliminary and per-

manent injunctive relief to enjoin the Defendants from enforcing certain provisions of the Milk Industry Regulation Act, as its application unfairly discriminates against Plaintiffs and results in a violation of the takings clause protected by the Fifth Amendment of the Constitution of the United States[1], and the dormant Commerce Clause.[2] Plaintiffs also seek a declaratory judgment on the constitutionality of the laws and regulations that govern the milk industry in Puerto Rico, particularly, the Milk Industry Regulation Act, Act No. 34 of June 11, 1957, 5 L.P.R.A. §§ 1092-1125 (Act No. 34"), as amended, and Regulation No. 1 of June 11, 1957 ("Regulation No. 1), as amended.

The Second Amended Complaint has six (6) causes of action, which are summarized below. The Court, however, has already ruled that Plaintiffs' allegations are colorable, potentially viable, and not frivolous in nature. *Vaquería Tres Monjitas, et al. v. Fabré Laboy, et al.*, ____ F. Supp. 2d ____, 2006 WL 2560486, *1-2 (D.P.R. September 1, 2006).

First Cause of Action: Plaintiffs challenge the constitutionality of Milk Regulation No. 1, as the margin of thirty cents ($0.30) provided to the industrial milk processors is insufficient to cover their costs, and "much less receive a reasonable return on their investment." Plaintiffs further allege that Defendants are not providing Plaintiffs a timely yearly review of the different margins

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[1] The Fifth Amendment of the U.S. Constitution provides in its relevant part, ". . . nor shall private property be taken for public use, without just compensation."

[2] Article 1, section 8[3] of the U.S. Constitution provides in its relevant part, Congress shall the power "[t]o regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes . . . "

and payments to be received pursuant to statutory requirements (yearly review of subsidized transportation from the farm to the factory on behalf of the farmers; subsidized price of raw milk to Indulac). *See* Docket No. 206 at p.p. 27 and 29. Plaintiffs move the Court for a ruling to declare either as applied or on its face, Milk Regulation No. 1 "an unconstitutional confiscation of plaintiffs' property." *Id.*

Second Cause of Action: Plaintiffs allege that the orders and decisions entered under Milk Regulation No. 1 constitutes a confiscation of plaintiffs' property without due process of law, and the orders and decisions taken as a whole force plaintiffs to "subsidize the entire milk industry, particularly, [Indulac] their most important competitor in the fluid milk market." *See* Docket No. 206 at p. 29. Plaintiffs also allege that Milk Regulation No. 1 imposes a higher purchase price on Tres Monjitas and Suiza Dairy of $0.66125 per quart for fresh milk, as opposed to the guaranteed minimum price for surplus milk fixed on Indulac $0.10 per quart (sounding clearly in violation of due process and equal protection, provided by the Fourteenth Amendment[3] of the U.S. Constitution). *See* Docket No. 206 at p. 31. Moreover, plaintiffs argue that the already fixed prices will not be amended under the proposed Milk Regulation No. 10. *See* Docket No. 206 at p. 32. (The prices have since been modified as to certain items but Plaintiffs insist on the constitutional infirmity.)

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[3] The Fourteenth Amendment of the U.S. Constitution 3 provides in its relevant part, ". . . No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws."

Third Cause of Action: Plaintiffs challenge the Administrator's interpretation of Milk Regulation No. 1, and Act No. 34, as it "violates the guarantee of equal protection of the laws" provided by the Fourteenth Amendment of the U.S. Constitution, as it discriminates between private fresh milk processors and Indulac, as they vigorously compete within the fluid milk market. *See* Docket No. 206 at p.p. 32-33.

Fourth Cause of Action: Plaintiffs allege that the orders issued by the Administrator only favors "in-state commercial interests (Indulac), over out-of-state interests (potential and actual competitors in the market for UHT milk), due to the artificially low subsidized prices" fixed to Indulac. *See* Docket No. 206 at p. 34. Plaintiffs argue that the Administrator's orders constitute a barrier against interstate trade in UHT milk and violate the "dormant" Commerce Clause of the U.S. Constitution, which is applicable to the Commonwealth of Puerto Rico. *See* Docket No. 206 at p. 35. Plaintiffs allege that the violation to the "dormant" Commerce Clause affects their interests. *Id.*

Fifth Cause of Action: Plaintiffs allege that the defendants have failed to prevent monopoly and unfair competition practices, and discrimination in several phases of the milk industry, from production up to the sale of milk, and its by-product to the consumer. *See* Docket No. 206 at p. 36. In sum, the defendants have failed to properly regulate Indulac by openly granting unfair advantage, to wit: (a) exclusive subsidize access to raw material; (b) exclusive producer of UHT milk in Puerto Rico; and (c) subsidized transportation services for acquiring the raw milk at plaintiffs' expense. *See* Docket No. 206 at p. 36. Moreover, the Administrator has failed to grant plaintiffs the requested licenses to

produce UHT milk, notwithstanding that plaintiffs meet the requirements for said license. Suiza Dairy argues that the Administrator has violated its due process, as the Administrator has failed to provide notice to Suiza Dairy of any type, nor has the Administrator furnished the opportunity to Suiza Dairy to show that it meets the requirements to obtain the license, all in violation of the Equal Protection Clause. *See* Docket No. 206 at p. 37.

Sixth Cause of Action: Plaintiffs seek a declaratory judgment under the Federal Declaratory Judgment Act, 28 U.S.C. §§ 2201, *et seq.*, finding that the decisions, acts and orders issued by the Administrator under Milk Regulation No. 1 are unconstitutional, on the following grounds: (a) confiscation of property, as the Administrator does not allow Plaintiffs to make a reasonable profit in their milk business, and recover real transportation costs; (b) by guaranteeing Indulac "an artificially low subsidized" price for the milk used by Indulac to produce the UHT milk, and allowing Indulac to enter into an open competition in the milk market, which is discriminatory and unreasonable, as it violates plaintiffs' due process of law rights; (c) deprivation of equal protection of laws by advancing information to a competitor; (d) violation to the "dormant" Commerce Clause for failure to provide economic protection to plaintiffs; and (e) failure to comply with the legislative intent of Act No. 34.

On October 31, 2005, Indulac filed a *Motion To Dismiss First, Fourth And Fifth Causes Of Action Under Rule 12(b)(1) And Request For The Court To Refrain From Exercising Its Jurisdiction As To The Other Causes Of Action Pursuant To The Burford Abstention* ("Indulac's motion to dismiss") (Docket No. 225), on the following grounds:

(a) The First Cause of Action should be dismissed as the "alleged takings claims is not ripe for adjudication," thus, the Court lacks jurisdiction to entertain it. *See* Docket No. 225 at p. 2.

(b) The Court should abstain from entertaining the Second, Third and Sixth Causes of Action "because doing so would require federal court interpretation of unclear state law regarding complex regulation of important state issues." *See* Docket No. 225 at p. 3.

(c) The Fourth Cause of Action should be dismissed as Plaintiffs lack standing to claim a violation to the dormant Commerce Clause, thus, the Court lacks subject matter jurisdiction over this claim. *See* Docket No. 225 at p. 2.

(d) The Fifth Cause of Action should be dismissed under Rule 12(b)(1) of the Federal Rules of Civil Procedure ("Fed.R.Civ.P."), "since the Eleventh Amendment[4] precludes the Court from addressing Plaintiffs' request for the Court to enjoin defendants to act pursuant to Act No. 34," the Puerto Rico Milk Industry Regulation Act ("Act No. 34"), 5 L.P.R.A. §§ 1092-1125. *See* Docket No. 225 at p. 2.

On October 31, 2005, the Secretary filed a *Motion To Dismiss The Second Amended Complaint And Motion Requesting Abstention And That The Court Deny The Plaintiffs' Motion For Injunctive Relief* (the "Secretary's motion to dismiss") (Docket No. 227). The Secretary moves the Court to dismiss and/or to abstain the

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[4] The Eleventh Amendment of the U.S. Constitution provides in its relevant part, "[t]he Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects fo any Foreign State."

Second Amended Complaint, and to deny the injunctive relief requested by Plaintiffs based on this Court's lack of subject matter jurisdiction under Rule 12(b)(1), and the complaint fails to state a claim upon which a relief can be granted under Rule 12(b)(6).

The Secretary also alleges that the instant case is not ripe for resolution as Plaintiffs have failed to exhaust the administrative or judicial remedies available to them "to challenge the legality and constitutionality of Regulation 1 and Act 34." *See* Docket No. 227 at p. 2. As to Plaintiffs' claim under the takings clause, the Secretary argues that if the Court is devoid of subject matter jurisdiction to entertain the constitutional challenge of Regulation No. 1 and Act No. 34, then it is unlikely that Plaintiffs' allegations under the Fifth Amendment will succeed on the merits.

As to the injunctive relief requested by Plaintiffs, the Secretary alleges that only two of the four requirements that would warrant the issuance of an injunctive relief are met, thus, Plaintiffs' relief must be denied. The Court notes, however, that the Secretary's arguments are based, in part, on the proposition that Plaintiffs may be entitled to damages on their claim of economic loss, thus, a "monetary compensation would provide a more that adequate remedy here." *See* Docket No. 227 at p. 3.[5]

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[5] Notwithstanding addressed below, the Court leaves the 5 request as to the absence of elements required under the injunctive relief under Fed.R.Civ.P. 65 for another day which is currently under Court advisement. However, the Court notes that "a deprivation of a [federal] constitutional right 'for even minimal periods of time unquestionably constitutes irreparable injury.'" *DeNovellis v. Shalala*, 135 F.3d 58, 71-72 (1st Cir. 1998) (citing *Elrod v. Burns*, 427 U.S. 347, 373 (1976).

On November 1, 2005, the PRDFA filed a *Motion Restating Motion To Dismiss As To Second Amended Complaint* ("PRDFA's motion to dismiss") (Docket No. 228), on the following grounds: (a) lack of jurisdiction, as the complaint "fails to state a federal constitutional claim amenable for resolution" by this Court; (b) this Court is precluded by the Eleventh Amendment from addressing Plaintiffs' request for the Court to enjoin defendants to act pursuant to Act No. 34;" (c) the alleged "takings" claim is not ripe for adjudication; (d) the alleged due process and equal protection claims which are based upon milk pricing discrimination against Plaintiffs constitute a challenge to the constitutionality of Act No. 34 "that attaches to legislative actions in the local economic sphere;" and (e) Plaintiffs do not have standing to challenge the dormant Commerce Clause. *See* Docket No. 228 at p. 2.

On November 18, 2005, Plaintiffs filed three pleadings: (a) Memorandum in opposition to Indulac's motion to dismiss (Docket No. 237); (b) Memorandum in opposition to the Secretary's motion to dismiss (Docket No. 238); and (c) Memorandum in opposition to PRDFA's motion to dismiss (Docket No. 239). On December 27, 2005, Indulac filed a reply to Plaintiffs' opposition (Docket No. 249). On January 27, 2006, Plaintiffs filed a surreply to Indulac's reply (Docket No. 257), and the Secretary filed a motion to join Indulac's reply (Docket No. 258).

In view of the fact that the arguments stated in the motions to dismiss filed by the Secretary, Indulac and the PRDFA are procedurally and substantially similar, the Court, for discussion purposes only, will address them jointly. Likewise as to Plaintiffs' memorandums in opposition. Based on these premises, the Court will pro-

ceed to consider the parties' arguments of procedural nature based on the Court's lack of subject matter jurisdiction under Rule 12(b)(1), and the Second Amended Complaint's failure to state a claim upon which a relief can be granted under Rule 12(b)(6).

**Applicable Law and Discussion**

A. Motion to Dismiss Standard under Fed.R.Civ.P. 12(b)(1).

"When a court is confronted with motions to dismiss under both Rules 12(b)(1) and 12(b)(6), it ordinarily ought to decide the former before broaching the latter." (citations omitted). *Deniz v. Municipality of Guaynabo*, 285 F.3d 142, 149 (1st Cir. 2002). "After all, if the court lacks subject matter jurisdiction, assessment of the merits becomes a matter of purely academic interest." 285 F.3d at 150.

Rule 12(b)(1) provides that a complaint will be dismissed if the court lacks subject matter jurisdiction. It is settled that the standard followed by the court when considering a dismissal request under Rule 12(b)(1), is that the court "must accept as true all well-pleaded factual claims and indulge all reasonable inferences in plaintiff's favor." *Viqueira v. First Bank*, 140 F.3d 12, 16 (1st Cir. 1998), as restated in *Rolón v. Rafael Rosario & Associates, Inc., et al.*, ____ F.Supp.2d ____, 2006 WL 2556408, *1 (D.P.R. August 31, 2006). To determine jurisdiction under Rule 12(b)(1), the court may also review the evidence on record, including affidavits and depositions, as opposed to a dismissal request under any other subsection of Rule 12(b). Once the jurisdiction of the court is challenged by the defendant through a motion to dismiss, "it is plaintiff's burden to establish that the court has jurisdiction." *Rolón*, 2006 WL 2556408, *1.

"Federal Courts are courts of limited jurisdiction," *Rolón*, 2006 WL 2556408, *1, thus, "this Court has the responsibility to police the border of federal jurisdiction" *Spielman v. Genzyme Corp.*, 251 F.3d 1 (1st Cir. 2001), and "must rigorously enforce the jurisdictional limits [standards] that Congress chooses, *Del Rosario Ortega v. Star Kist Foods*, 213 F.Supp.2d 84, 88 (D.P.R. 2002) (citing *Coventry Sewage Association v. Dworking Realty Co.*, 71 F.3d 1, 3 (1st Cir. 1995), as restated in *Rolón*, 2006 WL 2556408, *1.

In the instant case, the Secretary, Indulac and PRDFA allege that the Court lacks subject matter jurisdiction on the following grounds:

*The Takings Clause, Due Process of Law and Equal Protection*

The First Cause of Action challenge the constitutionality of Regulation No. 1 and Act No. 34, as it constitutes a taking of property without due process of law. The parties allege that this cause of action is not ripe of adjudication, thus, it should be dismissed, as the Court lacks jurisdiction. Plaintiffs allege that the case is ripe for adjudication under the *Williamson*[6] test, and *Texas v. United States*, 523 U.S. 296 (1998). PRDFA that Plaintiffs' constitutional challenge of Act No. 34 "attaches to the legislative actions in the local economic sphere." The Court disagrees.

The instant case is ripe for adjudication, simply because the prices have already been established, as opposed to prices that have not been established, thus, it is a matter of due process of law. Further, there are naked

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[6] *Williamson County Regional Planning Comm. v. Hamilton*, 473 U.S. 172 (1985).

questions of due process since the Plaintiffs are alleging that the pricing scheme is also not being timely entertained as required by statute. Moreover, the pricing proceeding established by Act No. 34 is not being achieved, as the end result shows an unfair advantage favoring Indulac, who is owned by the Government. This result constitutes a violation of the Takings Clause, which is clearly a naked question of federal Constitutional law.

After a review of the record, as permissible under the dismissal standard of Rule 12(b)(1), the Court finds that the instant case is ripe for adjudication, as the facts as pleaded, hinge on the actual events, as opposed and uncertain events and/or lack of due process required by the local statute. Hence, "equitable injunctive relief is the classic equitable remedy," *Morales Feliciano v. Rullán*, 378 F.3d 42, 50 (1st Cir. 2004), "to protect property rights against injuries otherwise irremediable," *K-Mart Corp. v. Oriental Plaza, Inc.*, 875 F.2d 907, 914 (1st Cir. 1989). *See also Vaquería Tres Monjitas, Inc.*, 2006 WL 2560486, *7.

*The Exhaustion of Administrative Remedies*

The Second, Third and Sixth Causes of Action should be dismissed as Plaintiffs have failed to exhaust the administrative remedies provided under Act No. 34. The Court disagrees, as the issue in this case hinges on Defendants' failure to comply with due process of law not as an issue of exhaustion of remedies.

First, the facts pleaded in the Second Amended Complaint are silent as to any pending administrative proceedings before a governmental agency or a local court. Second, it is well settled that when plaintiff alleges a violation of a constitutional right under 42 U.S.C. § 1983, there is no need to exhaust the administrative

remedies. *Monroe v. Pape*, 365 U.S. 167 (1961), *reversed on other grounds, Monell v. Department of Social Services of the City of New York*, 436 U.S. 658 (1978); *Ellis v. Dyson*, 421 U.S. 426, 432 (1975); *Patsy v. Board of Regents of the State of Florida*, 457 U.S. 496, 516 (1982) (the "exhaustion of state administrative remedies should not be required as a prerequisite to bringing an action pursuant to § 1983"). Moreover, after the Supreme Court's decision on *Monroe v. Pape*, "the circuits all adhere to the no-exhaustion rule in connection with state remedies." Nahmod, Sheldon H., 2 *Civil Rights And Civil Liberties Litigation*, § 9.13, Third Edition (1991).

In the instant case, the Secretary alleges that this Court is devoid of jurisdiction to entertain Plaintiffs' constitutional challenges to Regulation No. 1 and Act No. 34. However, Plaintiffs' complaint requests relief under 42 U.S.C. § 1983, thus, this is a federal question case, in which the exhaustion of administrative remedies is not required. Hence, this Court finds that it has subject matter jurisdiction to entertain the injunction application, and abstention under exhaustion is not a consideration at this time.

*The Dormant Commerce Clause*

The Fourth Cause of Action should be dismissed as Plaintiffs lack standing to bring this claim. The Court disagrees. *Prima facie*, the instant case is justiciable under *Walgreen Co. v. Rullán*, 405 F.3d 50 (1st Cir. 2005). Whether or not Plaintiffs have standing to claim a violation under the dormant Commerce Clause hinges on the evidence to be presented by Plaintiff to prove said claim. Plaintiffs claim that the orders issued by the Defendants as to the Ultra High Temperature ("UHT") only favors in-state commercial interests, such as Indulac, over out of state interests. Indulac's UHT product is lower than

the UHT milk from out of state due to the "artificially low subsidized prices" fixed to Indulac.[7] The Secretary argues that Plaintiffs' lack standing, as Plaintiffs' allegations fail to meet the "balancing test" under the dormant Commerce Clause, and the regulation that governs the milk industry in Puerto Rico does not have extraterritorial effect. Plaintiffs argue that the argument of lack of standing is premature, as the Court must assume that the allegations are true under the Rule 12(b)(1) dismissal standard.

After a careful review of the Fourth Cause of Action, and taking as true the well pleaded facts of the complaint, the Court finds that there is doubt as to whether or not Plaintiffs have standing to bring a claim under the dormant Commerce Clause. *See Alliance of Automobile Manufacturers v. Gwadosky*, 430 F.3d 30 (1st Cir. 2005), *cert. denied*, 126 S.Ct. 2034 (2006); *Walgreen Co. v. Rullán*, 405 F.3d 50 (1st Cir. 2005); *Grant's Dairy Maine, LLC v. Commissioner of Maine*, 232 F.3d 8 (1st Cir. 2000). In the event, Plaintiffs can show that Regulation No. 1 and Act No. 34 prohibits Plaintiffs to import or export milk, or even to produce UHT milk, then Plaintiffs have standing under the dormant Commerce Clause. The Court finds that, based on the dismissal standard of Rule 12(b)(1), Plaintiffs' claim is well pleaded and may be provable, thus, dismissal is for lack of stand-

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[7] The Court notes that Plaintiffs allege in the Fifth Cause of Action, that the Secretary has declined to issue them a license to produce UHT milk, while a licensed to produce the UHT milk has been issued by the Secretary to Indulac. The Defendant also allows the importation and sale of UHT in the market to compete with the fresh milk produced and distributed by Plaintiffs.

ing is not warranted at this stage of the proceedings.[8] Moreover, as long as Plaintiffs have a license application to produce UHT milk pending, there exists a potential cause of action since Plaintiffs may have valid plans to import the milk or the raw materials of the UHT frustrated by Defendants refusing to grant a license to process UHT milk in violation of the Equal Protection Clause.

*The Eleventh Amendment*

The Fifth Cause of Action should be dismissed under the Eleventh Amendment, as the Court is impaired to enjoin the Defendants to act pursuant to local Act No. 34. The Court wholly agrees with this argument. *See Pennhurst State School & Hospital et al. v. Halderman et al.*, 465 U.S. 89, 117 (1984), "a federal suit against state officials on the basis of state law contravenes the Eleventh Amendment when the relief sought has an impact directly on the State itself." However, Plaintiffs cause of action is under 42 U.S.C. § 1983, as opposed to state law.

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[8] Notwithstanding, the Court is conscious of the potential lack of standing allegation. However, to meet the Constitution's standing requirements, plaintiff must show:

> (1) It has suffered and "injury in fact" that is (a) concrete and particularized and (b) actual or imminent, not conjectural or hypothetical;
>
> (2) The injury is fairly traceable to the challenged action of the defendant; and
>
> (3) It is likely, as opposed to merely speculative, that the injury will redressed by a favorable decision.

*Iravedra v. Public Building Authority, et al.*, 196 F.Supp.2d 104, 115 (D.P.R. 2002). *See also Friends of the Earth, Inc. v. Laidlaw Environmental Services (TOC), Inc.*, 528 U.S. 167 (2000); *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560-561 (1992).

Without reaching the merits, it is well settled that the Eleventh Amendment defense is not applicable in an injunction application, when the only remedy requested even against a State actor in his official capacity, is an equitable injunctive relief. In *Mills v. State of Maine*, 118 F.3d 37, 54 (1st Cir. 1997), the Court, quoting *Seminole Tribe v. Florida*, 517 U.S. 44, 73 (1996), held that, "since our decision in *Ex parte Young*,[9] we often have found federal jurisdiction over a suit against a state official when that suit seeks only prospective injunctive relief in order to end a continuing violation of federal law." In the instant case, Plaintiffs are seeking a prospective injunctive relief against the Defendants to avoid insolvency but they are not seeking damages nor a monetary compensation. Hence, this Court finds that it has subject matter jurisdiction to entertain the injunction application.

Finally, the Secretary also argues that the injunction application should be dismissed, as it fails to comply with the injunctive relief requirements.[10] The factors to issue a preliminary injunction in this Circuit are: (a) irreparability of injury; (b) likelihood of merits success; (c) effect on the public interest; and (c) the "balance of 'relevant equities (most importantly, the hardship to the nonmovant if the restrainer issues as contrasted with the hardship to the movant if interim relief is withheld) . . .'"

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[9] 209 U.S. 123 (1908).

[10] Under the Declaratory Judgment Act, 28 U.S.C. §§ 2201-2202, the federal courts have "the power to declare the rights and other legal relations of any interested party seeking such declaration." 1 *Civil Rights And Civil Liberties Litigation*, § 5.02. As opposed to an injunction application, a "declaratory relief may be granted even though some other adequate remedy exists." *Id.*

*K-Mart Corp. v. Oriental Plaza, Inc.*, 875 F.2d 907, 914 (1st Cir. 1984) (citations omitted).

The Secretary further argues, that in the event the Court finds that it has jurisdiction to entertain this matter, Plaintiffs may be entitled to a damages award to recover on their economic loss, and this award may be translated into a monetary compensation. The Court disagrees with the Secretary's argument as to a possible damages award, and consequently, a monetary compensation to Plaintiffs. The Secretary's argument is bald and speculative, and unlikely to succeed as Plaintiffs have not claimed any damages in their injunction application. The Court further finds that the Secretary's argument is misplaced and unsupported from the facts pleaded in the Second Amended Complaint, hence, it is contrary to the mandated dismissal standard of Rule 12(b)(1).

After a careful review of the Second Amended Complaint, the Court finds that the facts alleged in the complaint are well pleaded. As stated above, the Court finds that Plaintiffs' allegations are colorable, potentially viable and not frivolous in nature. *Vaquería Tres Monjitas*, 2006 WL 2560486, *1. Moreover, as stated in our Order of September 1, 2006, the issue pending before the Court is a matter of "public interest." *Id.*[11] The Court also finds, after having examined the Second Amended Complaint in the light most favorable to Plaintiffs, construing the complaint liberally, taking all well pleaded facts as true, and drawing all reasonable inferences in favor of Plaintiffs, as we must in a motion to dismiss standard, *Viquei-*

[11] The Court cannot on one hand deny the consolidation of the preliminary injunction with the permanent relief stating that the case is one with "public interest," and then turn around and state that the case now lacks "public interest." The Court cannot engage in such flip-flop.

*ra v. First Bank*, 140 F.3d 12, 16 (1st Cir. 1998) as restated in *Rolón*, 2006 WL 2556408, *1, the Court has subject matter jurisdiction to entertain the constitutional challenges of Regulation No. 1 and Act No. 34, and any other subsequent order with similar constitutional requirements and/or procedural deficiencies, as alleged by Plaintiffs.[12]

B. Motion to Dismiss Standard under Fed.R.Civ.P. 12(b)(6).

"A complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). However, when opposing a Rule 12(b)(6) motion to dismiss, "a plaintiff cannot expect a trial court to do his homework for him." *McCoy v. Massachusetts Institute of Technology*, 950 F.2d 13, 22 (1st Cir. 1991). Thus, Plaintiffs must set forth "factual allegations, either direct or inferential, regarding each material element necessary to sustain recovery under some actionable theory." *Romero-Barceló v. Hernández-Agosto*, 75 F.3d 23, 28 n. 2 (1st Cir. 1996) (quoting *Googley v. Mobil Oil Corp.*, 851 F.2d 513, 514 (1st Cir. 1988). In sum, a claim shall be dismissed under Rule 12(b)(6) only if it appears beyond doubt that the pleader can prove no set of facts in support of the claim that would entitle the pleader to relief. *Conley*, 355 U.S. at 45. However, the court is not obligated to accept plaintiff's "bald assertions, unsupportable conclusions, periphrastic circumlocutions, and the like." *Aulson v. Blanchard*, 83 F.3d 1, 3

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[12] The Court notes that this case involves one of continuous shifting targets as the defendants continue to amend the regulations as the case progresses.

(1st Cir. 1996), as restated in *Padilla Román v. Hernández Pérez*, 381 F.Supp.2d 17, 22 (D.P.R. 2005).

A district court's dismissal of a claim under Fed.R.Civ.P. 12(b)(6) is reviewed *de novo* by the court of appeals. *Calderón Ortiz v. Laboy Alvarado*, 300 F.3d 60, 62-63 (1st Cir. 2002), as restated in *Rolón*, 2006 WL 2556408, *2. Thus, any order of dismissal shall be set aside, if the facts pleaded in the complaint, viewed in the light most favorable to plaintiff, justify a recovery under any applicable legal theory. *Padilla Román*, 381 F.Supp.2d at 22.

In the instant case, the parties allege that the Second Amended Complaint should be dismissed under Rule 12(b)(6), on the same grounds as those argued under Rule 12(b)(1). The arguments are indeed repetitious, hence, they are denied on the same grounds. *See* discussion of the dismissal standard under Rule 12(b)(1) *infra*. The Court finds that this is a federal question case under 42 U.S.C. § 1983, hence, the Court has original jurisdiction to entertain the same.

Based upon the most strict application of the motion to dismiss standard under Rule 12(b)(6), which is the applicable standard at this stage of the proceedings, "the Court is obligated to accept as true all well pleaded allegations." *Padilla Román*, 381 F.Supp.2d at 29. Hence, accepting as true all well pleaded allegations of the Second Amended Complaint, viewed in the light most favorable to Plaintiffs, the Court finds that the claims pleaded in the Second Amended Complaint are provable, justifiable, and a remedy may be justified under applicable legal theories. *Padilla Román*, 381 F.Supp.2d at 22. Hence, the motions to dismiss filed by the Secretary, Indulac and PRDFA are denied except as heretofore stated.

## Conclusion

In view of the foregoing, the motions to dismiss filed by the Secretary, Indulac and PRDFA (Docket entries No. 225, 227, 228), are **GRANTED** in part as to the Fifth Cause of Action, but limited as to granting an injunctive relief based on local law. Otherwise, the motions to dismiss are hereby **DENIED** on all other grounds.

**IT IS SO ORDERED.**

170 (4)

No. 10-74

# In The Supreme Court of The United States

JAVIER RIVERA AQUINO, SECRETARY,
PUERTO RICO DEPARTMENT OF AGRICULTURE, *ET AL.*,

*Petitioners,*

v.

SUIZA DAIRY, INC., *ET AL.*

*Respondents.*

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

## BRIEF IN OPPOSITION

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## QUESTIONS PRESENTED

The petition before this Court seeks review of a judgment by the Court of Appeals for the First Circuit affirming a preliminary injunction in a still ongoing case. The portion of the remedy to which petitioner objects has not been yet fully implemented. In that context, the substantive questions presented are:

1. Whether the Eleventh Amendment applies to the unincorporated territory of Puerto Rico as it does to any State of the Union.

2. Whether a federal court can order a territory that has decided to regulate its milk market, to provide, in the rates to be set prospectively for payment of milk by consumers, a charge to reconstruct the regulated entity's capital that was depleted by the unconstitutional actions of the territory, without violating the Eleventh Amendment.

## CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Supreme Court of the United States, respondent Suiza Dairy, Inc. ("Suiza") states that it is not a publicly held corporation that issues stock. Its parent corporation is Grupo Gloria Holding Corp., an entity not publicly held.

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## I. STATEMENT OF THE CASE

This complicated regulated market case is still pending final resolution before the U.S. District Court for the District of Puerto Rico. As of today, the case is nearly six years old, and it continues in its preliminary injunction phase, despite a docket consisting of more than 1600 entries. Many preliminary injunction issues remain unresolved. In particular, the remedy that petitioners submit is offensive to the Eleventh Amendment has not been fully implemented. *See* Pet. App. at 50a f/n 3. Neither the amount of the regulatory accrual remedy, nor its precise mode of calculation or the recovery schedule have been set. *See* U.S.D.C. Dkt. Nos. 1512, 1547, 1577, 1619, and 1662. *See also* Suiza's App. at A-2, A-13 to A-15.

This case arises out of the decision made by the Government of Puerto Rico to regulate the Puerto Rico milk market. The Puerto Rico Milk Regulatory Agency ("ORIL") forces the fresh milk processors to operate within a range controlled by ORIL. ORIL determines the price at which processors can purchase raw milk and the price at which they can sell finished product to their clients. *See* Pet. App. at 5a. Because of the *de facto* control of the dairy farmers over ORIL, the price of raw milk was kept high while

the price of processed fresh milk was kept low. *See* Pet. App. at 5a-6a, 91a, and 93a-94a.[1]

Acting on respondents' petition for a preliminary injunction, the District Court held 51 intensive evidentiary hearings over the course of one and a half years. On July 13, 2007 the District Court granted a preliminary injunction. *See* Pet. App. at 12a. The Court found that ORIL had committed numerous constitutional violations that are painstakingly detailed in the Court's ninety-five page Opinion and Order. The same contains 239 footnotes with specific references to the factual record developed.

In relation to the issues raised by the petition for certiorari, the District Court concluded:

> The regulatory system of ORIL has created for the fresh milk processors yearly losses that have *consistently diminished their capital base.* The normal regulatory way of dealing with this issue is by creating a capital account of "regulatory accrual" *that would add to the capital base the erosion experienced because of this regulatory system.* By providing in future rates a rate of return *over the capital plus the capital losses,* the companies could be made whole and be

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[1] Not a single factual determination of the District Court was ever challenged by petitioners *See* Opinion of the Court of Appeals, Pet. App at 3a f/n. 1.

> *provided the necessary recovery of cost and reasonable profit.* (Emphasis added, footnotes referring the record omitted).

*See* Pet. App. at 118a.

The District Court also found that:

> ORIL has failed to follow these principles and has intentionally squeezed plaintiffs between the gap of a fixed regulated price and an irrational high price for raw milk. ORIL has intentionally issued this administrative measure in order to protect Indulac[2] in the competition with the local fresh milk industry and the continental importers. The evidence shows, from admissions of the farmers, that ORIL's price fixing scheme is designed to fulfill these goals.

*See* Pet. App. at 168a.

Moreover, the Court found that ORIL continuously and arbitrarily changed its regulatory position in order to allow and disallow costs to manipulate figures and squeeze respondents between a high price for raw milk and an artificially low price for processed milk. *See* Pet. App. at 123a. The "lack of regulatory rules has been the

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[2] A milk processor controlled by the dairy farmers. *See* Pet App. at 81a-82a

instrument through which plaintiffs have been denied the recovery of their costs, as well as a 'fair profit' in the fresh milk business". *See* Pet. App. at 167a.

In order to address that situation, the preliminary injunction in essence orders ORIL to establish any further regulation and milk prices on the basis of scientific, non-discriminatory, rational and fair standards. Presumably, those standards will result in a fair evaluation of respondents' operational costs for purposes of cost recovery.

But as the District Court recognized, in a regulated market respondents also have the constitutional right to be allowed to receive a reasonable profit over the recovery of operational costs. That profit is calculated by ORIL by applying a rate of return percentage figure to the capital base of respondent. The undisputed evidence presented during the compliance hearings of this preliminary injunction is that respondents' combined capital stood at minus $5 million. *See* Pet. App. at 24a. This negative figure is the result of the capital base diminution arising out of ORIL's unconstitutional actions. *See* Pet. App. at 118a.

In order to reconstruct respondent's capital base and provide a rate of return over equity in prices going forward ("reasonable profit"), ORIL was ordered to adopt the customary method of capital reconstruction in regulated markets known as "regulatory accrual". This regulatory accrual takes

the form of an additional amount that respondents are allowed to charge their customers for processed milk during a set period of time. The capitalized total figure is added to the base of capital for purposes of applying the adopted return on equity percentage going forward. The outcome of those operations is the final price to be paid for processed fresh milk by the clients of respondents. After a certain period, the regulatory accrual remedy disappears from the milk price.

The preliminary injunction does not mandate ORIL "to allow respondents to recover a higher rate of return going forward." Pet. Brief at 4. The injunction does not set any particular rate of return. Rather, the injunction simply orders the adoption of adequate standards that will allow ORIL to "determine cost and fair profit return for all the participants in the Puerto Rico regulated milk market", Pet. App. at 197a, whatever those are.

The regulation promulgated by ORIL imposing a 1.5¢ surcharge over the price of milk but ordering respondents to deposit said portion of the price collected from their clients in a segregated account at ORIL is not a provision "[i]n compliance with the district court's order." Pet. Brief at 4. The District Court never ordered ORIL to become custodian of a portion of the milk price collected by respondents from their clients. ORIL decided to do so on its own thus precluding respondents' immediate access to a portion of the preliminary injunction remedy. *See* Suiza's App. A-4 to A-8.

As the Court of Appeals correctly indicated, according to the District Court's order, the price paid by the milk clients would be neither collected by government entities nor deposited in the Commonwealth's treasury. "Apart from the initial price order, no state action is required to implement this remedial scheme, which would, in no way, reach the coffers of the Commonwealth." *See* Pet. App. at 26a.[3]

Petitioners requested the Court of Appeals to retain the mandate. Suiza filed its opposition, Suiza's App. A-1 to A-15, and the Court returned the mandate by a unanimous vote.

## II. REASONS FOR DENYING THE PETITION

### A. There are no reasons justifying review of this interlocutory decision.

Ordinarily, this Court does not issue a writ of certiorari to review a decree of a circuit court of appeals on appeal from an interlocutory order. *American Construction Co. v. Jacksonville, Tampa and Key, W. R. Ry. Co.*, 148 U.S. 372, 384 (1893). This case presents no extraordinary circumstances that would justify issuing the writ before the final decree. *Hamilton-Brown Shoe Co. v. Wolff Brothers*

[3] It is simply to misconstrue the remedy to say, as the *Amici* Brief does, that the Court of Appeals approved of an order "compelling [Puerto Rico] to collect and deposit funds into a specific account earmarked for retrospective monetary relief" *See Amici* Brief at 3 and 8.

& Co., 240 U.S. 251, 258 (1916); *Denver v. New York Trust Co.*, 229 U.S. 123, 133 (1913). *See* also *Virginia Military Institute, et al. v. United States*, 508 U.S. 946 (1993). The petition does not even address this issue.

That finality rule is of particular importance in this case since the District Court is still in the process of implementing the preliminary injunction issued more than three years ago. As we have said before, the regulatory accrual remedy under attack by petitioners here has not been implemented in full, and key decisions regarding its operation remain to be made. An additional record is in the process of development. The Court should not enter into the issues raised by the petition on the basis of an incomplete record and without allowing the District Court to finish its business in connection with the remedy in question. Issuing the writ at this time will induce the inconvenience, litigation costs and delay in achieving ultimate justice that frequently accom any interlocutory appeals. *See Johnson v. Jones*, 515 U.S. 304, 309-310 (1995). *See* also E. Gressman et al., *Supreme Court Practice* 82 (9th ed. 2007).

### B. This case is not suited for this Court to decide now the narrow and local issue of whether the Eleventh Amendment applies to Puerto Rico.

This Court has never decided whether the Eleventh Amendment applies to the unincorporated territory of Puerto Rico to the same extent that it does to the States of the Union. That is an issue that goes to the core of the relationship between Puerto Rico and the United States. *See Downes v. Bidwell*, 182 U.S. 244 (1901); *Dooley v. United States*, 183 U.S. 151 (1901); E. Rivera Ramos, *The Legal Construction of Identity: The Judicial and Social Legacy of American Colonialism in Puerto Rico* (2001); J. Torruella, *The Supreme Court and Puerto Rico: The Doctrine of Separate and Unequal* (1985); J. Trias Monje, *Puerto Rico: The Trials of the Oldest Colony in the World* 36-51 (1997); C. Burnett and B. Marshall (eds.), *Foreign in a Domestic Sense: Puerto Rico, American Expansion and the Constitution* (2001); J. Kerr, *The Insular Cases: The Role of the Judiciary in American Expansionism* (1982); Katz, *The Jurisprudence of Legitimacy: Applying the Constitution to US Territories*, 59 U. Chi. L. Rev. 779 (1992); Terrasa, *The United States, Puerto Rico, and the Territorial Incorporation Doctrine: Reaching a Century of Constitutional Authoritarianism*, 31 J. Marshall L. Rev. 55 (1997).

This was not an issue in the Court of Appeals because, as petitioners correctly recognize, the Court of Appeals for the First Circuit has consistently

decided, for over a quarter century, that the Eleventh Amendment applies in full force to Puerto Rico. *See* Pet. Brief at 7-8, f/n 1. As demonstrated by the case petitioners themselves cite, *Ezratty v. The Commonwealth of Puerto Rico*, 648 F.2d 770 (1st Cir. 1981), that conclusion was reached with practically no explanation. *Id.* at f/n 7. But if this Court is to impose such a serious limitation to the power of Congress over Puerto Rico under the Territorial Clause of the U.S. Constitution, a thorough analysis of the unique political status of Puerto Rico will certainly be required. *Cf. Calero Toledo v. Pearson Yacht Leasing Co.*, 416 U.S. 663 (1974) (discussing the evolution in Puerto Rico's status since the end of the Spanish-American War in 1898).

To provide the remedy that petitioners seek, this Court cannot operate under the "assumption" that the Eleventh Amendment applies to Puerto Rico as petitioners invite it to do. *See* Pet. Brief at 7-8, f/n 1. This Court operated under that assumption in *Puerto Rico Aqueduct and Sewer Authority v. Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 n.1 (1993). But the question there was entirely different. The only matter that this Court had to decide, and decided in that case, was whether an order denying a motion by a state or a state entity to dismiss a civil action on grounds of immunity from suit in federal court, under the Eleventh Amendment, was immediately appealable under the collateral order doctrine. The Court of Appeals had responded in the negative and had dismissed that appeal on jurisdictional grounds.

This Court reversed, holding that there was no jurisdictional impediment to the consideration of the Eleventh Amendment claim of Puerto Rico in that context. But the Court of Appeals had not reached the merits of the Eleventh Amendment claim and this Court had no need to do so in order to resolve the jurisdictional issue before it.

That is certainly not a way out of this case. If, as petitioners submit, a portion of the preliminary injunctive remedy affirmed by the Court of Appeals should be annulled on the basis of the Eleventh Amendment defense of Puerto Rico, a holding that said amendment limits the power of Congress under the Territorial Clause of the Constitution needs to be made first.[4] For reasons already stated, this is hardly the case for such a narrow but difficult question to be entertained. *Cf. Harris v. Rosario*, 446 U.S. 651 (1980) (holding that Congress may treat

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[4] Consistent with its long standing position, the Court of Appeals here ruled on the merits of ORIL's Eleventh Amendment claim construing the same as it would have had the claim been made by a state. In that context, it is irrelevant that "[r]espondents have not disputed the proposition that Puerto Rico is entitled to sovereign immunity at any stage of this litigation." (Pet. Brief at f/n 1) since that determination is the cornerstone of the decision appealed. Furthermore, "... even if this were a claim not raised below, we would ordinarily feel free to address it, since it was addressed by the court below." *Lebrón v. National Railroad Passenger Corp.*, 513 U.S. 374, 379 (1995). There is no way of escaping the reach of what petitioners want this Court to rule in the context of this interlocutory appeal.

Puerto Rico differently than it does a state in public welfare programs because of the Territorial Clause).

### C. The decision of the Court of Appeals is consistent with the Eleventh Amendment precedents of this Court, since the injunction imposes no actual or potential monetary liability upon Puerto Rico.

The Court of Appeals explained very clearly why its decision was consistent with the Eleventh Amendment precedents of this Court. For the sake of brevity we abstain from repeating those arguments here and invite the Court to examine the analysis contained in the Court of Appeals' Opinion, Pet. App. at 24a-28a, and the Opinion of Judge Torruella concurring in the denial of *en banc* review, Pet. App. at 46a to 54a. The key element is that the monies of the remedy are strictly private in nature and that petitioners never argued that they are in any way public funds. *See* Pet. App. at 49a.

As the Court of Appeals correctly indicated:

> [Petitioners] provide no support for their contention that retrospective relief *that does not reach the state treasury* is barred by sovereign immunity. Rather, the cases cited by defendants, including *Edelman*, involve requests for retroactive compensation that would invariably come out of state treasuries. *See, e.g., id.*, at 667 ("[Relief sought] requires payment of state funds, not

> as a necessary consequence of compliance in the future with a substantive federal-question determination, but as a form of compensation...."); *Papasan v. Allain*, 478 U.S. 265, 279 (1986) (plaintiffs sought funds directly from the state to fund school districts).

*See* Pet. App. at 25a. Emphasis in the original.

Petitioners rely heavily on *Regents of the University of California v. Doe*, 519 U.S. 425 (1997). That case provides no support for petitioners' position. In *Doe*, plaintiff sought to obtain payment of damages from the State fisc of California. The disbursement for payment would have come from State coffers but for an indemnity agreement with the federal government that made the latter responsible for said payment. *Doe* stands for the proposition that if the State is obligated to pay retroactive damages from its own coffers, the fact that a subsidiary source of funds, such as an indemnity agreement or an insurance policy exists, does not defeat the Eleventh Amendment defense.

But that is not the situation here. The Government of Puerto Rico has not been ordered to pay one single cent, be it from its coffers or anywhere else, to respondents. This preliminary injunction simply provides that if the Government of Puerto Rico decides to continue regulating milk prices on the island (a choice Puerto Rico is free to make either way), then it has to regulate prices

prospectively providing for the reconstruction of respondents' depleted capital in order to allow them to recover costs and make a reasonable profit. There is absolutely no indication in the injunction that the price for milk that the consumers would be paying is *in lieu* of a payment that otherwise would come from State coffers. That is clearly distinguishable from the situation in *Doe* in which *but for* the indemnity agreement with the federal government, the State of California would have been responsible for the judgment sought by plaintiff. *See* Pet. App. at 49a-50a.[5]

It is precisely by looking "... to the substance rather than to the form of the relief sought," *Papasan v. Allain*, 478 U.S. 265, 279 (1986), as petitioners invite this Court to do (Pet. Brief at 9), that the Court of Appeals correctly reached the conclusion that its holding was not in opposition to this Court's holding in *Doe*.

*Green v. Mansour*, 474 U.S. 64 (1985) does not support the position of petitioners. Relying on *Quern v. Jordan*, 440 U.S. 332 (1979) plaintiffs in *Green*

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[5] To say, as *Doe* holds, that a state doesn't lose its immunity because the federal government pays *in lieu* of the state does not imply, as the *Amici* Brief suggests at p. 17, that the State can *transfer* its immunity to a private entity by agreeing voluntarily to pay in its place. A federal indemnity is not a transfer of federal immunity to the State. Similarly, a voluntary payment by the State on behalf of a third party may be a waiver of its immunity but not a transfer of the same to a non-sovereign. That argument by the *Amici* is a *non-sequitur*.

were seeking declaratory judgment that past actions of State officials violated federal law. But, at the time this remedy was sought, there was indisputably no ongoing violation of federal law. Without an ongoing violation of federal law no prospective remedy was possible. In that context, the declaratory judgment would only have served:

> ... as *res judicata* on the issue of liability, leaving to the State courts only a form of accounting proceeding whereby damages or restitution would be computed. But the issuance of a declaratory judgment in these circumstances would have much the same effect as a full fledged award of damages or restitution [against the State] by the federal court, the latter kind of relief being, of course, prohibited by the Eleventh Amendment.

*Green* at 73. At the time of the issuance of the preliminary judgment and as of today, there is a continuing violation of federal constitutional law in this case.

Puerto Rico's treasury is not compromised by this preliminary injunction now or in the future. If Puerto Rico were to deregulate the prices of milk, a decision that only Puerto Rico can take, the obligation to provide for a recapitalization remedy in the prospective rate would disappear. Whatever capital or revenue requirements respondents may then have, would be satisfied from the price they

charge for their product as determined by market forces. But even if Puerto Rico were to continue regulating the market and the increase in price would lead the consumers to reduce their purchases of milk, that would prolong the period the recapitalization of respondents' would take, but would not in any way compromise Puerto Rico's coffers. The preliminary injunction required Puerto Rico to prospectively set the price of milk, which it has decided to regulate, by the method customarily used to redress depleted capital problems in regulated markets. It does not require Puerto Rico to force consumers to buy milk, much less pay for milk with public funds if the consumers refuse to do so with their own.

### D. The decision of the Court of Appeals is not in conflict with those of other circuits.

Petitioners submit that the interlocutory decision of the Court of Appeals here is in conflict with decisions from several other circuits. That contention is incorrect.

*Esparza v. Valdez*, 862 F.2d 788 (10th Cir. 1988) deals with a claim for unemployment benefits to the State of Colorado. Colorado, as many other states, operated its unemployment benefits program under the Federal Unemployment Tax Act ("FUTA"), 26 U.S.C. §§3301-3311. That is a scheme by which the federal and state governments cooperate to provide

assistance to unemployed workers. As the Court correctly indicates:

> Under FUTA, the federal government helps States fund the cost of administering unemployment compensation programs while leaving most of the actual raising and all of the paying out of benefit monies to the States.

*Id.* at 789.

After recognizing that "... some district courts and one circuit have allowed plaintiffs to sue a State in federal court for recovery of past unemployment claims, principally on the grounds that the State's unemployment compensation fund is a special, segregated fund as distinguished from a general revenue fund", the Tenth Circuit rejected the operational validity of the distinction between one fund and the other. The Court held that said distinction between "general" or "special revenue" fund (both holding public monies), from which the State would have to pay unemployment benefits, does not preclude application of the Eleventh Amendment.

*Paschal v. Jackson*, 936 F.2d 940 (7th Cir. 1991) is a very similar case dealing also with a claim for retrospective unemployment benefits. Again, plaintiffs were seeking disbursement of public funds segregated in a special account. The consideration for which public funds would be disbursed was the

past unemployment status of claimants. Since public funds were to be disbursed, the Seventh Circuit, like the Tenth, found irrelevant for Eleventh Amendment purposes the particular account in which the state kept these public funds. The Court found irrelevant "the source of State funds" provided that the disbursement was of "state funds", which unemployment benefits always are.

*Cronen v. Texas Department of Human Services*, 977 F.2d 934 (5th Cir. 1992) is also a similar case which deals with a claim for retrospective welfare, instead of unemployment, benefits. In this case, Cronen sought restoration of past food stamp benefits that, according to him, were denied improperly. In short, Cronen's claim was based on his legal right to have State funds paid to him, on account of meeting certain poverty related criteria. As it is pertinent here, the Court simply upheld an Eleventh Amendment defense against the disbursement to plaintiff of State funds although those were of federal origin. Interestingly, the Court intimates that plaintiff's argument may have been successful had it filed suit, not against the State itself but as respondents here, against the State officials in their official capacity. *See Cronen, supra* at 938.

In *Florida Association of Rehabilitation Facilities, Inc. v. Florida Department of Health and Rehabilitative Services*, 225 F.3d 1208 (11th Cir. 2000) a claim on behalf of disabled people was made against State officials. The District Court directed

defendants to correct their Medicaid reimbursement plan prospectively and retrospectively. The Court of Appeals reversed the part of the judgment that required the State to pay money for pre-judgment violations. Again, these Medicaid funds were undoubtedly State funds that had to be disbursed by the State to redress pre-judgment claims. As the Court itself said, "... we note that the judgment clearly does contemplate the payment of State funds to redress prior inadequate reimbursements." *Id.* at 1220.

Finally, in *Ernst v. Rising*, 427 F.3d 351 (6th Cir. 2005) the Court was dealing with a claim by certain state court judges that the State of Michigan was violating the Federal Equal Protection Clause by giving more favorable retirement benefits to other state court judges. The retirement system of the State was a product of State legislation, run by State officials and funded by the State treasury. The Court upheld the Eleventh Amendment defense finding irrelevant the fact that the State retirement funds in question were kept in a State "pocket" different than that of the State's general funds.

These cases are clearly distinguishable from the case at bar. Unemployment, welfare, Medicaid, disability and retirement pensions are all obligations of the State payable with State funds regardless of the origin of said funds or the particular account in which they are kept. All of the above cases reject those origin and fiscal deposit distinctions when it comes to the Eleventh Amendment.

But that is not at all the situation of this case. Before Puerto Rico decided to regulate milk prices, retailers and consumers would pay respondents for processed milk at a price set by market forces. The money paid did not constitute State funds but money paid by a private citizen to a private entity in exchange for goods. After Puerto Rico decided to regulate the price to be paid, in the exercise of Puerto Rico's police power, that money continued to be paid in exchange for the processed milk of respondents and did not alter its strictly private character at all. It continued to be money paid for milk belonging to private parties and not State funds of any sort. Petitioners nor *Amici* cite any authority for the proposition that whenever the State engages in rate making, the nature of the payment for the regulated commodity changes from private money to "State funds". *See Amici* Brief at 18.

In essence, for years, the milk consuming public received the benefit of the unduly low price of fresh milk caused by ORIL's unconstitutional actions. Now, it is that public's private money that will be used to procure constitutionally valid prospective rates through recapitalization. In a deregulated market that result would be achieved through a price hike freely determined by respondents. But since Puerto Rico continues committed to price regulation, the regulatory accrual remedy becomes necessary. But the liability for that remedy does not

fall upon the government but upon the milk buyers, as it would in a deregulated market.[6]

### E. The decision of the Court of Appeals is correct.

As Suiza has shown above, the Court of Appeals did not rule as it did because the monies in question here did not come "directly from the general treasury". Pet. Brief at 16 and *Amici* Brief at 2. It ruled as it did because the funds in question do not come directly **nor** indirectly from the general treasury since they are strictly private monies paid to private parties in order to buy from them a particular commodity.[7] But there are other reasons why this petition should be denied. In compliance

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[6] The preliminary injunction does not require ORIL to do anything other than take into consideration the regulatory accrual elements in setting the new price going forward. ORIL is not required by the preliminary injunction to interfere or participate in the collection of monies, nor deposit them in a government account or distribute the same. The money continues to be collected by respondents ORIL on its own has ordered respondents to send back to ORIL for "deposit" the regulatory accrual monies. *See ante* at 13-15 and Suiza's Motion in Opposition to Motion for a Stay of Mandate, Suiza's App at A-4 to A-10 The 1 5¢ surcharge was not "judicially imposed", *Amici* Brief at 12, but unilaterally determined by ORIL in that same administrative order.

[7] There is no basis for the statement by *Amici* at 18 that " . the reason the milk surcharge would not reach the public fisc is that the injunction itself directs the funds elsewhere in advance." The price of milk always goes from the consumer through the retailer to the processors, not to the government with injunction or without it.

with Rule 15(2) of this Court we mention them briefly.

### 1. The regulatory accrual remedy is not barred by the Eleventh Amendment under *First English Evangelical Lutheran Church v. County of Los Angeles*, 482 U.S. 304 (1987).

The District Court held that the February 2006 price order issued by ORIL in the middle of this litigation constituted an unconstitutional taking of Suiza's property. *See* Pet. App. at 171a. The Court ordered that unconstitutional regulatory taking to cease by, among other things, reconstructing the erosion that the same had caused on Suiza's capital from the year 2003 which was the base year of the order in question. Suiza submits that compensatory remedies for temporary takings, even if they are (unlike here) paid with State monies present no Eleventh Amendment problem in light of the holding of *First English Evangelical Lutheran Church v. County of Los Angeles*, 482 U.S. 304 (1987). That is the reading afforded to that case by many[8] including

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[8] *See* for example, Fallon, R. H. & Meltzer, D. J., *New Law, Non-Retroactivity, and Constitutional Remedies*, 104 Harv. L. Rev. 1731, 1825 & n. 536 (1991) (referring to *First English* by saying " the Court rejected the United States' position that, in light of sovereign immunity, the just compensation clause should not be interpreted to require a monetary remedy"); Grant, E., *A Revolutionary View of the Seventh Amendment and the Just Compensation Clause*, 91 NW. U. L. Rev. 144, 201 (1991) (asserting that in *First English* "The Court thus

the Court of Appeals for the First Circuit. *See Parella v. Retirement Board*, 173 F.3d 46, 57 (1st Cir. 1999) (Lynch, Cir. Judge) (recognizing while discussing the prospective– retrospective conundrum of the Eleventh Amendment that in *First Lutheran* the Supreme Court "firmly established" that "the Takings Clause also requires just compensation for temporary takings (which would seem to be irreducibly retrospective)").[9] *See Tenoco Oil Co. v. DACO*, 876 F.2d 1013, 1027 n.20 (1st Cir. 1989). ("The Supreme Court... has held that damages are retrospectively available for the period of 'temporary' takings, *i.e.*, regulatory takings ultimately

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"recognized" our first reformulated postulate associated with sovereign immunity independent of congressional action, citizens have a judicially enforceable right to just compensation from the government, by virtue of the Constitution"), Merrill, T.W., *The Landscape of Constitutional Property*, 86 Va. L. Rev. 885, 981 & n.351 (2000) (citing *First English* for the proposition that " .the Takings Clause has been held to incorporate a self-executing waiver of state and federal sovereign immunity against claims for monetary compensation"), Jackson, V. C., *Seductions of Coherence, State Sovereign Immunity and the Denationalization of Federal Law*, 31 Rutgers L.J. 691, 724 n.126 (2000) (citing *First English* for the proposition that "notwithstanding sovereign immunity, the Constitution 'dictates' a remedy for takings of property"); Jackson, V. C., *The Supreme Court, the Eleventh Amendment, and State Sovereign Immunity*, 98 Yale L.J. 1, 115 & n.454 (1998) (stating that *First English* strongly suggests that States lack sovereign immunity from just-compensation claims in federal court).

[9] This categorical statement by Judge Lynch on behalf of a unanimous Court of Appeals in *Parella* is difficult to reconcile with her dissent in the case before this Court.

invalidated as unconstitutional by the courts."). *See* also, *Lucas v. So. Carolina Coastal Council*, 505 U.S. 1003, 1011-1012 (1992); *Tahoe-Sierra Preservation Council v. Tahoe Reg. Planning*, 535 U.S. 302, 347 (2002), (Rehnquist, CJ, dissenting) and *Stop the Beach v. Florida*, 130 S. Ct. 2592, (2010) (Kennedy J., concurring).

**2. The remedy objected to by petitioners is indispensable to set prospective rates. As such it is not a retrospective remedy.**

Without the regulatory accrual to reconstruct depleted capital any prospective rate will be insufficient to provide a reasonable profit to respondents. The remedy is thus prospective.

In a free milk market, respondents' revenue and resulting profit would come from charging for their products as high a price as the market would bear. Whatever revenue requirements respondents may have, would come directly from the amount they get from the consumer according to the laws of offer and demand.

But in Puerto Rico's regulated milk market the laws of offer and demand have been displaced. The margin between cost and price to the consumer is determined by the government. The government is constitutionally required to set a margin that provides the regulated entity an opportunity to make a "reasonable" profit. *See* Pet. App. at 164a-171a and authorities therein cited.

To provide for the recovery of cost is a rather simple operation for ORIL. The amount of allowed costs divided by the units of product to be sold produces a price that permits respondents to break even. But the problem comes in determining what additional amount respondents should receive in order to make a "reasonable" profit. After ORIL has provided a cost recovery price, it calculates the reasonable profit by multiplying a preselected percentage of return ("ROE") by respondents' combined capital.

Both elements of the profit calculation are important. An underestimated ROE percentage provides an insufficient profit margin. But the same happens with an underestimated capital base. *X* percentage of 10 is always less than *X* percentage of 100. A negative capital base produces no profit at all.

The February 2006 ORIL price order, which has as a regulatory base respondents' operational numbers for the year 2003, eliminated valid costs incurred by Suiza in an arbitrary, irrational and discriminatory manner in order to turn an operational loss into a profit. *See* Pet. App. at 110a-111a.

These actions provoked a substantial depletion of respondents' capital. *See* Pet. App. at 118a. In a free market, that depletion would probably result in a substantial increase in prices. But that is not a

solution available to respondents in Puerto Rico's regulated milk market.

It is easy to understand what would happen with the District Court's prospective regulated market remedy if the regulatory accrual starting with the depleted base year 2003 is not allowed. Not even ORIL denies that in a regulated market, Suiza is entitled to prospectively recover costs *and* make a reasonable profit. The first step in the latter direction is to determine the percentage of ROE that Suiza should receive for a milk production facility operating under the economic conditions of Puerto Rico. But, as we have seen, the percentage figure is only half the story. The actual prospective profit to be received by Suiza varies enormously with the same return on equity percentage figure depending on the capital base to which that figure is going to be applied. Suiza's present capital base has been eroded so severely that a negative capital number results.[10] In other words, for Suiza to actually recover prospectively a reasonable profit in addition to its costs, its regulatory equity base has to be positive and real, that is, reconstructed to what it would have been today but for the intentional, unconstitutional confiscatory actions of ORIL. If

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[10] Pet App at 24a. Even ORIL's expert witness, Dr Ronald W Cotterill, recognized that " .and on the other hand of the balance sheet they had total liabilities plus equity equal, by definition, equal to those total assets, and at that time a net worth was a negative $5 million, so that was part of that side of the balance sheet" (Transcript of February 17, 2009 hearing, p 8, lines 24-25 to p 9, lines 1-4).

Suiza is to recover the necessary percentage of ROE over an unconstitutionally eroded regulatory equity base, Suiza would not be recovering prospectively its constitutionally mandated revenue requirement. The regulatory accrual remedy of the District Court is thus prospective inasmuch as it is indispensable to prospectively remedy ORIL's unconstitutional actions.

If "...relief that serves directly to bring an end to a present violation of federal law is not barred by the Eleventh Amendment even though accompanied by a substantial ancillary effect on the state treasury", *Papasan v. Allain*, 478 U.S. 265, 278 (1986), then such a relief when, the state treasury is in no way compromised, is unobjectionable.

The contention that this relief is prospective because it is necessary to rebuild respondents' capital base is not, as petitioners suggest, one that could almost always be made when a court awards retrospective monetary relief. *See* Pet. Brief at 16.

The reconstruction of the capital base is an issue here simply because respondents operate within a regulated market. It is in a regulated market that the "reasonable profit" results directly from having an adequate capital base allowed by the Regulator as a necessary investment for the regulated activity. In a free market, the concept of "reasonable profit" plays no role since every entity seeks to maximize its profit and charge for its product as much as the market will bear. In a free market environment,

whatever revenue requirements for capital reconstruction, or otherwise, respondents may have, would be satisfied from the maximum price for their product they can extract from the consumer. In short, the argument that the remedy is prospective because without it no reasonable profit is possible prospectively, is one that can be made only by the very small number of entities that operate within regulated markets of this same sort.

### 3. ORIL is precluded by waiver from raising any Eleventh Amendment defense.

The agreement entered into between ORIL's expert and the experts for respondents constitutes a waiver by ORIL of its Eleventh Amendment defense.

During the month of August 2008, compliance hearings on this preliminary injunction were to be held before the District Court. At the behest of the Court the expert working for ORIL and the experts working for Suiza met with the purpose of narrowing the differences between the parties in connection with the last price order and proposed regulation. *See* U.S.D.C. Dkt. No. 1002 and U.S.D.C. Dkt. No. 1004. Also, *see* U.S.D.C. Dkt. No. 1164.[11]

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[11] The District Court stated in an order, denying the request to stay the compliance hearings, U.S.D.C. Dkt. No. 1164, p. 3 " on August 25 and on August 26, 2008 the experts after a long conference signed an agreement which simplified the compliance hearings as to rate of return. (Docket No. 1002, Minute, Docket 10[0]3, Experts Agreement)."

As expected by the District Court, a meeting between the experts produced agreements in several crucial issues substantially narrowing the differences between the parties. That agreement was reduced to writing and delivered to the District Court with the signatures of the experts. The Court entered the agreement into the docket. U.S.D.C. Dkt. No. 1003. (Transcript of August 26, 2008 hearing, p. 17, lines 14-25 to p. 18, lines 1-3). Although the actual percentage value of the return on equity to be used for each of the operating years between 2003 and 2007 was not agreed to, the parties did agree on the methodology for the calculation of the regulatory accrual and most importantly for the use of that result for the reconstruction of the present capital base of Suiza, over which a return on equity going forward would be applied. U.S.D.C. Dkt. No. 1003, Experts' Agreement, par. 1 (c), incorporating a table entitled "Estimated Regulation Accruals and Adjusted Capital base: 2003-2007". After the agreement, all the experts have used that methodology to reconstruct Suiza's capital. Transcript of February 17, 2009 compliance hearing, p. 11, lines 9-13. ORIL's expert witness admitted:

> Q. And if I look at the reconstruction of capital that you have done in this document, you're still - or as you always did - using the regulatory accrual to reconstruct captain [sic], right?

A Yes.[12]

...

Q. Now, going to capital, we need to reconstruct capital by capitalizing the regulatory accrual at the end of the exercise, right?

A. At some point in the exercise, yes.[13]

During a hearing held on January 12, 2009 the District Court indicated to the parties that the remaining controversies would be limited to those not already resolved in the experts' agreement.[14] Lastly, during yet another post injunction evidentiary hearing, ORIL's counsel accepted that the use of the regulatory accrual as the correct method to calculate Suiza's present capital base was agreed to. Transcript of compliance hearings of February 16, 2009, p. 11, lines 9-13. ("...but during the course of the discussions between the experts, I conceded on, when was it, Thursday that the capital base issue was, and the methodology to get to the capital base, was agreed").

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[12] Transcript of hearing held on February 18, 2009, p 25, lines 22-25 to p 26, line 1.

[13] Transcript of hearing held on February 18, 2009, p 45, lines 14-15, and p 69, lines 3-6

[14] Transcript of hearing held on January 12, 2009, p 41, lines 23-25 to p. 42, lines 1-4

ORIL cannot now come and raise an Eleventh Amendment defense against the regulatory accrual. ORIL has already accepted that, without the regulatory accrual, Suiza's present capital base cannot be correctly recalculated and thus Suiza cannot obtain the constitutionally mandated revenue requirement going forward. ORIL stipulated almost all of the regulatory accrual calculation elements. ORIL's action constitutes a recognition that the regulatory accrual remedy is prospective in nature and its acceptance of the same in the expert's agreement constitutes a waiver of any Eleventh Amendment defense it may have had in connection with the same.

A waiver of immunity can occur (1) when there is a clear declaration by the State that it intends to submit itself to the jurisdiction of a federal court; (2) by consent to or participation in a federal program for which waiver of immunity is an express condition; or (3) by affirmative conduct in litigation. *Clark v. Barnard*, 108 U.S. 436 (1883); *Lapides v. Board of Regents*, 535 U.S. 613 (2002); *Welch v. Texas Department of Highways and Public Transport*, 483 U.S. 468 (1987); *Nevada Department of Human Resources v. Hibbs*, 538 U.S. 721 (2003). Consent by conduct in litigation may occur when the state affirmatively complies with a court's implementation order. *Garrity v. Sununu*, 752 F.2d 727 (1st Cir. 1984). Voluntary entry into an agreement may also have the effect of waiving immunity through conduct. *New York State Ass'n. v. Carey*, 596 F.2d 27 (2d Cir. 1979); *Kozlowski v. Coughlin*, 871 F.2d 241, 244 (2d Cir. 1989).

### 4. ORIL created absolutely no record for its contention that it is an "arm of the State" for Eleventh Amendment purposes.

As demonstrated by f/n. 22 of Suiza's Brief before the Court of Appeals, Suiza specifically preserved the argument that ORIL had created no record before the District Court to support the contention that it was an arm of the State. ORIL had to develop a record on that issue. *See Ainstworth Aristocrat International Party v. Tourism Company*, 818 F.2d 1034, 1038 (1st Cir. 1987); *Figueroa v. Aquino*, 863 F.2d 1037, 1044 (1st Cir. 1988); *Fresenius Med. Care v. Puerto Rico & Caribbean Vascular Center Corp.*, 322 F.3d 56, 61 (1st Cir. 2003) *cert. den.* 540 U.S. 878 (2003). Failure to develop this record is fatal to ORIL's belated Eleventh Amendment argument.

Other circuits have expressly stated the need to develop a record on the arm-of-the-state issue. *See Gray v. Laws*, 51 F.3d 426 (4th Cir. 1995); *Pikulin v. CUNY*, 176 F.3d 598 (2d Cir. 1999) (remanding because "defendant should develop a record sufficient to allow the district court to consider fully [defendant's] relationship to the state."); *Gragg v. Kentucky Cabinet for Workforce Development, et al.*, 289 F.3d 958 (6th Cir. 2002) ("defendants have pointed to nothing on the record, and we have been unable to find anything on the record that would establish that they are arms of the state entitled to the protection of the Eleventh Amendment"); *East Central Health District v. Brown*, 752 F.2d 615 (11th

Cir. 1985) (District Court's denial of dispositive motion affirmed since the record did not establish an adequate factual basis to determine that defendant was an arm of the state).

5. **This is not a matter of exceptional importance requiring this Court's intervention especially at this stage of the proceedings.**

The principles embodied in the Eleventh Amendment are certainly important. But the Eleventh Amendment is not compromised in any way by the decision of the Court of Appeals. Petitioners have cited no authority for the proposition that a monetary award coming in the form of an increase in the price of goods paid for by the consumer to a private entity in the context of a regulated market compromises "directly or indirectly" public funds.

Petitioners and *Amici* are mistaken in alleging that this remedy equals a federal court ordering the imposition of a tax on citizens to pay damages. As recognized by the Court of Appeals, "...whether Puerto Rico could levy a special tax to compensate Tres Monjitas and Suiza is not the issue before this court". *See* Pet. App. at 27a. Monies collected by the government on account of a tax are State funds no matter the nature of the public purpose for which they are going to be used. But the regulated price of milk goes up and down for many reasons and those price changes cannot be qualified as tax imposition

or tax relief measures. They are changes in the amount paid by the public to a private entity whenever the public buys a commodity. Simply, rate making and tax imposition and collection are two entirely different government activities. The analogy does not work.

Finally, the impact of this decision is limited to the narrow realm of regulated markets. All the obligations of the Commonwealth of Puerto Rico under the injunction would disappear if Puerto Rico were to deregulate the prices of milk today. The decision to regulate or not to regulate the market is Puerto Rico's alone. But deregulation means that revenue will depend on the vagaries of the free market, reconstruction of regulatory capital would be meaningless and respondents would be obligated to fend on their own for their revenue needs. That is the case for all claimants outside the narrow realm of regulated markets. The decision of the Court of Appeals has no impact in free market situations where most of the Eleventh Amendment issues arise.

## V. CONCLUSION

There are no valid reasons for this Court to issue the writ of certiorari to review an interlocutory decision of the Court of Appeals in a still ongoing case particularly where the remedy under attack has not even been fully implemented. It is not even clear that petitioners here are covered by the Eleventh Amendment. The Eleventh Amendment does not apply because no government monies are implicated

here in any way and any "retrospective liability" falls upon the private resources of the milk buying public. The remedy is consistent with the rulings of this Court and there are no conflicts with decisions from other circuits. This case has no impact outside the limited realm of regulated markets.

The petition for certiorari should be denied.

Respectfully Submitted,

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August 26, 2010

**Interlocutory Appeal No. 07-2240;**
**Interlocutory Appeal No. 07-2369**

**United States Court of Appeals**
**For the First Circuit**

Interlocutory Appeal No. 07-2240

VAQUERIA TRES MONJITAS, INC.;
SUIZA DAIRY, INC.
Plaintiffs-Appellees

v.

JUAN R. PEDRO-GORDIAN, in his official capacity as Administrator of the Office of the Milk Industry Regulatory Administration for the Commonwealth of Puerto Rico
Defendant-Appellant

Interlocutory Appeal No. 07-2369

VAQUERIA TRES MONJITAS, INC.;
SUIZA DAIRY, INC.
Plaintiffs-Appellees

v.

SALVADOR RAMAIREZ, as Secretary of the Department of Agriculture for the Commonwealth of Puerto Rico
Defendant-Appellant

MOTION IN OPPOSITION
TO MOTION FOR STAY OF MANDATE

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MOTION IN OPPOSITION
TO MOTION FOR STAY OF MANDATE

Plaintiff/Appelle Suiza Dairy, Inc. ("Suiza") opposes the petition to stay the mandate filed by the Milk Industry Regulatory Administration of the Commonwealth of Puerto Rico and the Secretary of Agriculture of the Commonwealth of Puerto Rico (hereinafter jointly "ORIL" by the Spanish acronym of the Administration). The injunction ORIL appealed was issued in the summer of 2007. ORIL's brief on appeal was not filed until September of 2008. The preliminary injunction of the District Court was affirmed unanimously by a panel of this court. ORIL's re-hearing petition was also denied unanimously. ORIL's re-hearing *en banc* petition was denied with only one dissent. As of today, the preliminary injunction remains unenforced and ORIL's effort to keep it that way continues. The petition to stay the mandate should be denied for the reasons outlined

below.

## I – ORIL's petition for a writ of certiorari before the Supreme Court does not present a substantial question within the meaning of FRAP 41(d)(2)(A).

### A. There is no substantial 11th amendment issue.

There is no possibility of an 11th Amendment problem here because, as the panel recognized, the district court's preliminary injunction does not require the payment of any money – let alone any retrospective damages – from the public fisc of Puerto Rico. The district court's preliminary injunction is directed at ORIL, the Commonwealth's milk regulator, and it ordered ORIL to create a new pricing structure for the processing and sale of milk that affords the plaintiff milk processors a reasonable rate of return to be obtained from the milk buying public. After trial hearings lasting for more than three years, the district court found that the old ORIL pricing structure was confiscatory – it violated the processors' rights under the Takings, Due Process, and Equal Protection Clauses, as this Court affirmed.

The injunction requires no payment of money out of the treasury of Puerto Rico. Rather, the injunction mandates the setting by ORIL, the milk industry regulator, of a new pricing structure that does not violate the plaintiffs' constitutional right to a reasonable rate of return. One element of the new

price structure created by ORIL is the addition to the retail and wholesale prices of 1.5 cents – the "regulatory accrual" – per quart of milk to make up to the processors the multi-million dollar loss in capital experienced since 2003 on account of ORIL's confiscatory, unconstitutional pricing regime. The deficit in the plaintiff processors' capital will thus be made up over time, going forward, by the payments of Puerto Rico's milk consumers: every time they buy a quart of milk, they will be paying a price, 1.5 cents (or whatever amount is finally determined as part of the payout schedule) of which is repayment to the processors of the artificially low price of milk that the consumers enjoyed for years under ORIL's previous, unconstitutional price structure. This 1.5 cents per quart is paid by the consumer to the retailer (e.g., a supermarket) at the cash register; that money is in turn passed in the normal course of business by the retailer to the plaintiff milk processors. ORIL has no intervention in this collection process. This money part of the price of milk, has never and does not now, belong to the government, but to Suiza.

The only reason that some of the regulatory accrual funds is currently in the control of the government of Puerto Rico, is because ORIL has on its own and under no federal compulsion, intervened in the regular flow of money in the milk trade.

ORIL was required by the injunction to put a constitutionally consistent set of price regulations in place in 30 days. ORIL took over a year to enact and file with the court a new set of again constitutionally

deficient regulations. Without calculating the amount of the regulatory accrual, much less determining a payout period, ORIL decided to allocate for regulatory accrual purposes the amount of 1.5 cents per quart, an amount added to the price of milk to be paid by consumers and retailers. But ORIL then proceeded on its own to intentionally obstruct the district court's order by issuing an administrative directive to the plaintiff milk processors, requiring them to turn over the 1.5 cents per quart to ORIL. See Dkt. No. 1190-2,pags. 17-18.("Since the total sum of the compensation has not been determined by the court, **we hereby create, by virtue of the regulations herein, a fund for the eventual payment of such losses** ... The contribution for the abovementioned compensation shall be determined by the Administrator through an Administrative Order and shall be withheld and deposited in a special account in compliance with the orders it receives from the administrator of this agency in this regard.".(Emphasis added). ORIL deposited these funds in a separate, dedicated account, and is apparently holding them hoping to indefinitely prevent enforcement of this year's old preliminary injunction. That is, ORIL has itself effectively stayed the enforcement of the district court's preliminary injunction by seizing from the plaintiffs some of the fruits of the same, fruits to which plaintiffs are constitutionally entitled by the now affirmed order of the district court.

But what is crucial here is that the money ORIL is ordering plaintiffs to deposit with ORIL is money that comes from the retailers and consumers that buy

the milk Suiza produces and goes to Suiza directly. Furthermore, ORIL is requesting from Suiza remittance of that money not because the district court required ORIL to do so but because ORIL decided on its own to prevent Suiza's access to the money, as a way of defeating the immediate relief sought by the district court.

In order to support its Eleventh Amendment argument, ORIL intentionally created the impression in oral argument that the federal injunction issued by this court required ORIL to go out and collect money for regulatory accrual purposes, keep it in a fund and pay Suiza from it. (Mr. Hill: "The nature of the bar is whether the District Court can say to the state go, whether it comes from your coffers or not, go and collect a certain amount of money and pay back in a equitable relief claim." Transcript p. 5;[1] Mr. Hill: "However, to go back and say, and to tailor the remedy and say "go back and collect it from your, from the people, from the consumer, that your Honor I believe violates the Eleventh (11th Amendment)." Transcript, p. 6.) In describing the remedy Mr. Hill said: "Well here it would be collected by ORIL, be placed in an account and then delivered to the plants." Transcript, p. 6. At p. 10 of the Transcript, Mr. Hill said: "However, the tailoring of the equitable remedy is you, a state official, must go to the consumer and collect this money and pay it."

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[1]A transcript of the oral argument before this Court was made and filed with the District Court at Dkt No 1512-1

Those misrepresentations continue today. See ORIL's motion to stay the mandate at p. 8. (...the District Court's Opinion and Order forces the state to collect money in order to pay the plaintiffs their purported profits.")

An exchange between Judge Howard and counsel for Suiza during oral arguments clarified this issue.

JUDGE HOWARD:

Counsel, can I just ask you one factual question. I want to make sure that I understand what you said. The District Court did not order the agency to collect the regulatory accrual? It was the agency that told you to submit it to them?

MR. ESCALERA:

Yes.

JUDGE HOWARD:

After the District Court order was issued.

MR. ESCALERA:

Yes. Because, –

JUDGE HOWARD:

Ok. I thought that's what you said. I just want to be sure.

In short, the core of ORIL's 11th Amendment argument (although insufficient) is a money handling mechanism created by ORIL itself and not by the preliminary injunction of the district court.

When the district court eventually enforces its preliminary injunction, this money in the regulatory accrual account will be returned by ORIL to the plaintiff milk processors from whom ORIL seized it. Suiza will continue to collect from its clients (as it does now) the milk money and retain all of it, including the rest of the regulatory accrual money to which it is entitled, if any. Those actions will have no effect on the public fisc of Puerto Rico, because the money in the account as well as that collected in the future is not Puerto Rico's money – it is the property of the milk processors from whom ORIL seized it. That money is no more the property of the state than was the money deposited in a state court's interpleader registry in *Webb's Fabulous Pharmacies Inc. v. Beckwith,* 449 U.S. 155, 160-61 (1980). Thus neither the preliminary injunction, nor this Court's decision sustaining it, implicates the 11th Amendment because the money in ORIL's regulatory accrual account is not part of Puerto Rico's fisc, but is instead money ORIL seized from the plaintiff milk processors – money they received, at 1.5 cents per quart, from retailers to whom they sold processed milk under the new ORIL pricing regime mandated by the decision of the district court.

The dissent at p. 25 erroneously says:

> Under the regulatory accrual mechanism, the money collected from consumers goes into a special account in the FFIL that is controlled and administered by ORIL for eventual disbursal to plaintiffs. And all monies stored in the FFIL are, as a matter of Puerto Rican law, considered depositories of the Commonwealth. This is plainly relief that reaches the state fisc.

First, the "regulatory accrual mechanism" described by the dissent was created by ORIL not by the federal order. Second, ORIL could have ordered **all the revenues** of Suiza's milk sales to be deposited in an ORIL's fund "for eventual disbursal" to Suiza and no one would argue that such order had the effect of turning those moneys into Commonwealth's money.

Furthermore, the dissenting opinion mistakenly speculates that the Commonwealth of Puerto Rico may at some point be liable for the regulatory accrual moneys. See dissenting opinion at p. 23-24 ("And if this mechanism failed – if, for instance, consumers bought less fresh milk in response to the raised prices and the regulatory accrual failed to accumulate the significance sums needed to repay plaintiff – there is no indication ORIL would not still be on the hook for plaintiffs' loss profit.") Not only there is no indication whatsoever in the preliminary injunction to support this speculation but the same is plainly wrong. The

only way that the regulatory accrual money would stop flowing to plaintiffs is if every consumer in Puerto Rico were to stop buying milk. A decrease in the amount of milk consumers only entails a longer period for regulatory accrual recovery or price accommodations every time the price fluctuates because of changes in the cost structure. But even if all consumers were to stop buying milk that simply means that there are no more milk revenues of any kind, regulatory accrual included, coming to plaintiffs. The government would not have to pay plaintiffs for the revenue they now have ceased to receive for milk nobody is buying. The government will not have a milk market to further regulate. The Puerto Rico milk industry would have simply disappeared. But the point is that the government is not "on the hook" for the regulatory accrual moneys coming only from milk sales even in such a doomsday scenario.

B. There is no substantial *Williamson* question.

At p. 9 of its motion to stay the mandate ORIL says:

> Under Williamson[2] and its progeny, a federal court, in takings cases, would have to wait until the claimant ran the **state court** gamut to seek just compensation for the losses from the state courts, in the first instance in order

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[2] *Williamson County v. Hamilton Bank*, 473 US 172 (1985)

> to determine whether the federal court should grant just compensation, in the last instance. (Emphasis added.)

This Court itself has recognized that that is not at all the *Williamson* mandate. In *Tenoco Oil Company v. DACO,* 876 F.2d 103 (1st Cir. 1989) this court said:

> The Supreme Court has ruled that "a claim that the application of government regulations effects a taking of a property interest is not ripe until the **government entity charged with implementing the regulations has reached a final decision regarding the application of the regulations** to the property at issue. *Williamson Planning Commission v. Hamilton Bank,* 473 US at 186. (Emphasis added)

Subsequently, the *Tenoco* court went on to discuss the difference between finality at the administrative level (not at all an issue here) and the requirement to exhaust state judicial remedies. See *Tenoco* at p. 1025. Under *Williamson*, what is required is finality in the administrative decision not exhaustion of state judicial remedies.

Lastly, the remedies granted to Suiza are not exclusively the result of confiscation but also the result of Due Process of Law, Equal Protection and Dormant Commerce Clause violations.

II – This is an appeal from a preliminary injunction that has never been stayed but remains unenforced. This situation damages Suiza, the party that has prevailed at all stages in this litigation.

A preliminary injunction has immediate effect unless stayed at some point. This Court of Appeals has authority to stay the effects of a preliminary injunction. See USCS Fed Rules Civ Proc R 62. That remedy was never requested by ORIL. The reason is simple. ORIL has been successful in delaying enforcement of the injunction without having to prevail in a petition for stay. The District Court's opinion documented in detail ORIL's discriminatory animus against Suiza. See Dkt. No. 480.That animus has not changed and is causing substantial harm to Suiza.

The regulatory accrual remedy that should have been in place since the summer of 2007 is indispensable to grant Suiza a constitutional remedy going forward. The **undisputed** finding of fact number 54 of the District Court says:

> The regulatory system of ORIL has created for the fresh milk processors yearly loses that have **consistently diminished their capital base**. The normal regulatory way of dealing with this issue is by creating a capital account of "regulatory accrual" that **would add** to the capital base the erosion experienced

> because of this regulatory system. By providing in future rates a rate of return over the capital plus the capital loses, the companies could be made hold and be provided the necessary recovery of cost and reasonable profit. (Emphasis added, footnotes omitted). See Appellant's Addendum, pp. 140-141.

As found by the District Court and as explained at p. 32-33 and 45-50 of our brief, Suiza's capital has to be reconstructed in order for a reasonable rate of return to be applied and be capable of producing a reasonable profit. The calculation of the regulatory accrual has not been done and presently Suiza receives a rate of return over a depleted capital, an operation which is incapable of producing the constitutionally mandated reasonable profit. This capital reconstruction is a mathematical calculation the elements of which were agreed to by the experts for the parties. That agreement was reduced to writing and delivered to the District Court with the signatures of the experts. The court entered the agreement into the docket. See Appelle's Appendix, pp24-26 (transcript of August 26, 2008 hearing pp17, lines 14-25 to p. 18, lines 1-3). But Suiza's capital for the application of any rate going forward continues undermined.

In short, although the injunction continues in full force and effect, ORIL's petition for retention of the mandate will be used before the District Court as an excuse to continue postponing the urgently needed

recapitalization of Suiza and even consideration of many other pending issues. There is no reason to allow ORIL that opportunity in connection with the preliminary injunction that should have been fully enforced in 30 days and is still pending enforcement almost 3 years later.

**III – Under 28USC1254(1) certiorari review by the Supreme Court of a non-final judgment of a Court of Appeals is particularly unlikely.**

It has been well settled for years that although the Supreme Court has jurisdiction to do so under 28 US Code §1254(1), ordinarily the Supreme Court "...should not issue a writ of certiorari to review a decree of the Circuit Court of Appeals on appeal from an interlocutory order, unless it is necessary to prevent extraordinary inconvenience and embarrassment in the conduct of the cause." *American construction Company v. Jacksonville, Tampa and Key, W.RY.*, 148 US 372, 384 (1893). Except in extraordinary cases, "...the writ is not issued until final decree." *Hamilton-Brown Shoe Company v. Wolff Brothers and Company*, 240 US 251, 258 (1916). As indicated by Justice Scalia in *Virginia Military Institute et al v. United States*, 508 US 946:

> We generally await final judgment in the lower courts before exercising our certiorari jurisdiction. [Citations omitted]

See also *Brotherhood of Locomotive Firemen and Enginemen v. Bangor*, 389 US 237, 328 (1967).

Since this court is going to remand this case to the District Court for further proceedings, review by the Supreme Court at this stage is highly unlikely. No legitimate purpose will be served by a stay of the mandate.

In San Juan, Puerto Rico, this 19th day of March, 2010.

CERTIFICATE OF SERVICE

I hereby certify that on this same date, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to all attorneys of record.

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No. 10-74

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IN THE

# Supreme Court of the United States

JAVIER R. AQUINO, SECRETARY, PUERTO RICO DEPARTMENT OF AGRICULTURE, ET AL.,

*Petitioners,*

v.

SUIZA DAIRY, INC.;
VAQUERÍA TRES MONJITAS, INC.

*Respondents.*

**On Petition for a Writ of Certiorari to the United States Court of Appeals for the First Circuit**

## BRIEF IN OPPOSITION OF RESPONDENT VAQUERÍA TRES MONJITAS, INC.

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## CORPORATE DISCLOSURE STATEMENT

Vaquería Tres Monjitas, Inc. ("Tres Monjitas") is a for profit privately held corporation. Tres Monjitas has no parent company and no wholly owned subsidiary that has issued shares to the public.

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## RESPONDENT VAQUERÍA TRES MONJITAS, INC.'S BRIEF IN OPPOSITION

The petition is based on two underlying false assumptions: (1) the district court ordered Commonwealth agencies to impose a tax on consumers as damages for past constitutional violations; and (2) Puerto Rico would be liable to pay a monetary judgment if that purported tax were unsuccessful. Neither of these assumptions are supported by the record. And, once these faulty assumptions are dispelled, which can be done in short manner, the petition seeks nothing more than review of a factbound, interlocutory appeal

The facts of this case are unique and extreme. The Commonwealth of Puerto Rico has total control over its milk market, including control over respondents' prices, costs, and profits. Respondents cannot change either the amount that they pay for raw milk or charge to consumers for processed milk without government approval. The district court found that financially interested private citizens had captured control of government agencies and the Government was forcing respondents to operate their businesses at a financial loss, threatening their financial solvency.

After finding likely violations of the Takings, Due Process, and Equal Protection Clauses, the district court issued a preliminary injunction designed to stabilize the milk industry. In part, the district court required petitioners to create a temporary mechanism that would allow respondents to rebuild their capital bases so as to avoid bankruptcy.

The district court, however, did not order petitioners to tax consumers and did not order any monetary relief, much less any monetary relief from the Commonwealth's treasury. Indeed, the district court provided that petitioners could use any "available mechanism of [their] choosing," including allowing respondents to earn a higher prospective rate of return. Pet. App. 197a. The Commonwealth chose to allow respondents to increase the price of milk going forward by 1 5 cents per quart.

In addition, there is no indication that the Commonwealth would be potentially liable for monetary damages if the market would not sustain the 1.5 cents price increase. Judge Torruella, who wrote the panel's decision, expressly stated that it would be "pure speculation" to suggest that the Commonwealth could be "legally, practically or potentially" liable to respondents. *Id.* at 52a (Torruella, J., concurring in the denial of rehearing en banc). The court of appeals held that no state funds would be used and, as Judge Torruella explained, petitioners never "*argued on appeal that the monies raised by the regulatory accrual are public in nature.*" *Id.* at 49a (emphasis in original). Accordingly, because state funds are not implicated and the Commonwealth is not even potentially liable for any monetary payment, the court of appeals held that the Eleventh Amendment does not prohibit the preliminary injunction.

When the case is properly viewed, its significance dims. There is no widespread application to other States and no suggestion that courts can force a State to tax its citizens to pay for monetary damages. Nor is the case inconsistent with the precedent of

this Court or any circuit Indeed, petitioners do not cite one case in which an Eleventh Amendment violation was found when no state funds were at risk and the State was not even potentially liable for payment.

Furthermore, even assuming counter-factually that a split could be divined from petitioners' cases, the petition presents an exceedingly poor vehicle for this Court's review. As the court of appeals explained, the record at this stage is unclear. No permanent injunction has been issued and how the preliminary injunction will work in practice is unknown. Additional threshold legal questions such as the applicability of the Eleventh Amendment to Puerto Rico and to Takings claims have yet to be worked out. In fact, the court of appeals did not even decide whether the preliminary injunction was retroactive; the court simply assumed so. Even if the Court were interested in addressing the Question Presented, there is no good reason for the Court to grant the petition at this time.

## COUNTERSTATEMENT OF THE CASE

1. Respondents Tres Monjitas and Suiza Dairy, Inc. (collectively the "milk processors") purchase raw milk from dairy farmers, process the milk and sell the fresh milk to the public. At one time, there were over a dozen fresh milk processors in Puerto Rico. Today, respondents are the only fresh milk processors left.

Milk production in Puerto Rico is cyclical. The production is "heavily dependent upon the changing temperature, leading to instability in the seasonal yield of milk and, consequently, waste during months

of higher production." Pet. App 5a. The unstable production cycle led to tension between the dairy farmers and the milk processors and made the consistent supply of milk difficult. In 1957, Puerto Rico created the Office of the Milk Industry Regulation Administrator for the Commonwealth of Puerto Rico ("ORIL" by its Spanish acronym), an agency within Puerto Rico's Department of Agriculture, to "regulate all aspects of the Puerto Rican milk market." *Id.* at 78a.

At the same time ORIL was created, Puerto Rico also created the Milk Industry Development Fund ("FFIL" by its Spanish acronym), a government entity designed to promote Puerto Rico's fresh milk industry. *Id.* at 78a-79a. FFIL owns and operates Industria Lechera de Puerto Rico, Inc. ("Indulac"). Indulac processes ultra high temperature milk ("UHT milk"), "a type of milk that does not require refrigeration prior to opening." *Id.* at 4a. ORIL denied Suiza's application to process UHT and thus Indulac was the "sole entity in Puerto Rico authorized to process [UHT]." *Id.* Indulac's UHT milk "competes directly with the fresh milk produced" by the respondent milk processors. *Id.*

Originally independent entities, now "[b]oth the FFIL and Indulac are entities under the full control of the dairy farmers." *Id.* at 79a. In addition, "[t]he FFIL pays for ORIL's Administrator's automobile and other expenses" and "the Administrator of ORIL was also the Chairman of the Board of Indulac." *Id.* at 78a, 79a. The three entities share the same building. *Id.* at 79a.

As part of its regulation of the milk industry, ORIL set the minimum price that the milk

processors were required to pay dairy farmers for raw milk and set the maximum price that the milk processors could charge consumers for the fresh milk they processed. ORIL kept the price of fresh milk "low to make it affordable for consumers. The price of the raw milk, however, was kept high, based on ORIL's determinations regarding the farmers' costs of production and their reasonable expectations of profits." *Id.* at 5a-6a.

ORIL also required the milk processors to purchase all of the raw milk produced by the dairy farmers. The Puerto Rican fresh milk market, however, does not support processing all of the produced milk, leading to surplus raw milk. To avoid waste, ORIL required the milk processors to sell all of their surplus milk to Indulac. "Under ORIL's pricing system, Indulac purchased this surplus raw milk from the processors at a price significantly below the price that the processors paid the dairy farmers for their non-surplus raw milk." *Id.* at 6a.

In the mid-1980s, Indulac began using the surplus raw milk to process UHT. "Essentially, by mandating that plaintiffs pay a high price for raw milk and then requiring them to sell the surplus of that same milk to Indulac at a substantially lower price, ORIL created a scheme in which Tres Monjitas and Suiza were forced to subsidize Indulac, their competitor." *Id.* at 6a. Without this subsidy, Indulac would not have been able to compete with UHT milk imported from the United States. *Id.* at 6a-7a. "And, since Indulac was able to purchase its raw milk at a deflated price, UHT milk became significantly less expensive than fresh milk—a phenomenon unique to

Puerto Rico—causing Indulac's UHT milk to begin to dominate the Puerto Rican milk market." *Id.* at 7a.

Unlike for the milk processors, ORIL did not impose a maximum price for which Indulac could sell UHT. Because Indulac purchased its milk at a "deflated price" and had no restriction on the price for which it could sell UHT, Indulac's "profit margin ...soar[ed], while the processors struggled." *Id.* at 7a. "By the year 1998, Indulac was aggressively marketing UHT and devoting as much surplus milk as possible to its production." *Id.* at 94a-95a.

Although ORIL set the prices for raw milk, ORIL accepted the figures provided by Indulac without any hearing or examination. Thus, Indulac, which is under "full control of the dairy farmers," determined the "dairy farmers' costs and what constituted reasonable profits." *Id.* at 7a. Even during this litigation, ORIL relied solely on Indulac's figures to determine how much Indulac should pay for surplus raw milk. *Id.* at 8a. Additionally, ORIL's estimates were based on "clearly outdated economic figures" that failed to consider the "tremendous increase in prices of essential production elements" and the "consistent trend of reduced [milk] production." *Id.* at 9a. "Such determinations as to [the milk processors'] production costs, the price of raw milk, and the price at which they could sell fresh milk to consumers, allowed ORIL to control the milk processors' rates of return." *Id.*

Exacerbating the milk processors' financial condition, ORIL began to change the regulations governing the milk processors without any forewarning. ORIL, for example, did not "publish its rules of cost analysis," or "adopt a consistent and

scientific measurement of shrinkage, which represents the volume of milk regularly lost in the processing stage and is required for an accurate measurement of total production." *Id.* at 8a-9a. ORIL also failed to "follow a consistent standard in determining whether to allow income reductions for returns of product, . . . discounts to agents and promotions, and for the costs and fees of professional experts utilized by [the milk processors] to enable compliance with regulations." *Id.* at 9a.

As a result of ORIL's regulatory scheme, the milk processors began to operate at significant financial losses. ORIL refused to consider the milk processors' losses in setting future rates and continued to force the processors to operate at a loss.

2. Facing insolvency, the milk processors filed suit against petitioners, the Secretary of Agriculture and the ORIL Administrator, in their official capacities, in the United States District Court for the District of Puerto Rico in 2004. Later, both Indulac and the Puerto Rico Dairy Farmers intervened to assert additional defenses against the milk processors' claims.

The milk processors contended that ORIL's regulatory scheme violated the Due Process, Equal Protection and Taking Clauses of the United States Constitution and sought a preliminary injunction. Petitioners moved to dismiss the complaint based, *inter alia*, on Eleventh Amendment immunity, contending that the milk processors were seeking monetary damages. The district court rejected petitioners' argument, holding that "[i]n the instant case, [the milk processors] are seeking a prospective injunctive relief against [petitioners] to avoid

insolvency but they are not seeking damages nor a monetary compensation." *Id.* at 214a

a. After three years and fifty-one evidentiary hearings, the district court issued a preliminary injunction. The district court determined that the dairy farmers were using the Puerto Rican Government to try to bankrupt the milk processors. The court concluded that the dairy farmers wanted "to consolidate in their hands the control of the whole industry." *Id.* at 82a. The court explained that the dairy farmers' efforts to "eliminate[e] the fresh milk processors" continued while this lawsuit was pending and included "participation of officials of the Government of Puerto Rico involved directly and indirectly in the milk industry and its price setting scheme." *Id.* As the district court found, "[t]he more desperate the financial condition of the fresh milk processors, the easier for the dairy farmers to acquire or eliminate them." *Id.*

The district court found that petitioners had "intentionally squeezed plaintiffs between the cap of a fixed regulated price and an irrational high price for raw milk. . . . in order to protect Indulac. . . ." *Id.* at 168a. In addition, the record demonstrated "a pattern of lack of standards, change in standards with unfettered discretion, use of stale figures, and lack of an appropriate standard as to fair rate of return in the regulations set by the regulator." *Id.* at 192a. The court thus concluded that petitioners likely had violated the Equal Protection, Due Process, and Takings Clauses. *Id.* Because of petitioners' actions, the court found that the Puerto Rican milk industry was on the verge of collapse. Finding that respondents' continuing, independent

operation was in the public interest, the district court issued preliminary injunctive relief. Pet. App. 107a, 193a-194a.

b The district court's preliminary injunction attempted to stabilize the milk industry and prevent the bankruptcy of the milk processors. The district court required Indulac to pay the same price as the milk processors for raw milk. *Id.* at 196a. In addition, the court required ORIL's Administrator to conduct an economic study of Puerto Rico's milk market and "put into effect non-discriminatory, rational and scientific regulatory standards that will allow him to determine costs and fair profits return for all the participants in the Puerto Rico regulated milk market." *Id.* at 197a. The court also required the new system to have a mechanism to deal with losses that may occur between periods of review. *Id.*

Finally, and as relevant here, the district court ordered the creation of "a temporary mechanism that will allow the processors to recover the new rate of return" from 2003 (the beginning period of the "taking") until the new regulatory regime is implemented. *Id.* at 197a. The court allowed ORIL to determine the rate of return and how to implement the temporary mechanism, stating that "[t]he Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of his choosing." *Id.* The district court did not order any payment of money.

c. ORIL chose to implement the temporary mechanism by allowing the milk processors to increase the price of milk by 1.5 cents per quart. The milk processors collect this increase directly from the consumers through individual milk purchases.

While petitioners have proposed a regulation that would require the milk processors to turn over the funds from the price increase to ORIL, that regulation, has not yet taken effect. *See* Proposed Regulation No. 12 (Docket Nos. 938-4 & 1190-2), *Vaqueria Tres Monjitas, Inc.* v. *Laboy*, No. 04-1840 (D.P.R.). Thus, the milk processors currently retain control over funds received pursuant to the price increase.

4. Petitioners appealed to the First Circuit, contending that ORIL's price increase violates the Eleventh Amendment's prohibition on retrospective monetary awards. In a unanimous decision, the court of appeals rejected petitioners' argument because "[t]he damage the Eleventh Amendment seeks to forestall is that of the state's fisc being subjected to a judgment for compensatory relief." *Id.* at 26a (quotation marks and citation omitted).

The First Circuit held, under the facts of this case, "the money in question would come directly from consumers of milk in Puerto Rico. . . . [I]t would be neither collected by government entities nor retained in [Puerto Rico's] treasury." *Id.* Since "no state action is required" for the individual consumer transactions, ORIL's temporary mechanism and the remedial scheme "would, in no way, reach the coffers of the Commonwealth," and the Eleventh Amendment did not preclude the district court's equitable relief. *Id.* The court found no support for the proposition that the Eleventh Amendment bars relief "*that does not reach the state treasury*" and affirmed the district court. *Id.* at 25a (emphasis in original). Accordingly, the court did not reach the

question of whether the district court's order could be considered retroactive. *Id.* at 24a.

5. The court also rejected petitioners' subsequent motion for rehearing en banc. Chief Judge Lynch dissented from the denial because she believed that state funds were at risk and that, if ORIL's temporary price increase failed, ORIL might be considered liable for monetary payments. *Id.* at 64a (Lynch, C.J., dissenting from the denial of rehearing en banc). The remainder of the court voted to deny rehearing en banc.

Judge Torruella concurred in the denial of rehearing en banc and wrote separately to dispel Judge Lynch's description of the price increase. Judge Torruella explained, "there is simply no indication in the record or in the Regulations adopted by ORIL that an eventual judgment ordering disbursal of the monies raised pursuant to the regulatory accrual would be satisfied by public funds." *Id.* at 49a (Torruella, J., concurring in the denial of rehearing en banc) Indeed, as Judge Torruella noted, petitioners never even "*argued on appeal that the monies raised by the regulatory accrual are public in nature.*" *Id.* (emphasis in original). Judge Torruella further emphasized that "*[n]either the Commonwealth nor ORIL have been adjudged responsible for contributing funds to the special account.*" *Id.* (emphasis in original). Judge Torruella thus explained that "the precise compensation that Plaintiffs will be entitled to receive has not been determined as of yet" and the suggestion that the Commonwealth may bear some subsidiary monetary liability is "beyond speculation"

on the present record.[1] *Id.* at 50a n.3; *see also id.* at 52a ("[I]t is pure speculation to state that the Commonwealth is legally, practically or potentially" liable to the milk producers.).

Judge Torruella concluded that the panel had properly considered, "from a practical perspective, the Commonwealth's immediate and ultimate liability," and its decision was "consistent with settled precedent that examines an entity's entitlement to sovereign immunity through the prism of the financial burden actually or potentially imposed on the state." *Id.* at 51a, 53a. As there is no threat to the monetary interests of Puerto Rico, Judge Torruella explained, the court rightly affirmed the district court. *Id* at 54a.

## REASONS FOR DENYING THE PETITION

The petition should be denied because the court of appeals' decision does not raise any issue of national importance, is consistent with this Court's precedent, and does not create a split of authority among the circuits on the Question Presented. Moreover, even if the Court were interested in the Question Presented, myriad factors make this case a poor vehicle for this Court's consideration.

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[1] Both Chief Judge Lynch and Judge Torruella assumed that all funds collected from consumers were deposited in a state-administered account designated for payment to the milk processors. However, ORIL's proposed regulation creating this account has not been implemented. For approximately the last two years, the milk processors have retained control over the funds collected pursuant to the price increase.

## I. THE PETITION DOES NOT RAISE ANY ISSUE OF NATIONAL IMPORTANCE.

The court of appeals decided this case under a unique factual scenario that is not widely applicable to the domestic States. The Commonwealth controls the milk industry. ORIL determines the price at which milk processors must purchase raw milk, forces the milk processors to purchase all available raw milk—regardless of their needs or capacities—and dictates the price at which the processors will sell the milk. According to the district court, ORIL's price scheme forced the milk processors to take annual losses and threatened their solvency. *Id.* at 118a. Unlike typical private companies, because the Commonwealth has total control over the milk processors' prices, costs, and profits, they had no way to adjust their businesses to recoup prior losses and stave off bankruptcy.

The district court faced the task of crafting effective prospective injunctive relief under exceptional circumstances. Recognizing that merely ensuring a fair rate of return at some future date would not resolve the milk processors' financial insolvency, the court ordered petitioners to implement a "temporary mechanism" that would allow the milk processors to rebuild their capital bases. The district court left the details of the "temporary mechanism" to petitioners, but suggested that a higher prospective rate of return would accomplish this directive. *Id.* at 197a. Rather than give up regulatory control, however, the *Commonwealth itself* decided to allow respondents to charge an additional 1.5 cents per quart of milk.

As the facts demonstrate, the district court did *not* order any monetary relief, much less order the Commonwealth to impose a tax to pay a judgment, as petitioners mistakenly suggest. Because the Commonwealth has total control over the private companies, it could have ensured the milk processors' financial solvency by, for example, prospectively reducing its regulation or eliminating the maximum price charged to consumers. Such relief would not even arguably be considered retroactive monetary relief. In fact, there is no question that the district court could have struck down the Commonwealth's entire pricing scheme and, consistent with *Ex parte Young*, 209 U.S. 123 (1908), prospectively enjoined petitioners from setting price controls, a far more intrusive remedy than the price increase the Commonwealth chose here.

Moreover, in the context of the regulatory scheme, even the Commonwealth's chosen relief cannot be considered retroactive monetary relief. Only where the Government has total control over a private company would the company's attempt to restore its lost capital through consumer transactions require any government action. In the ordinary case, a company could always increase prices or decrease expenses to recoup past operating losses. Such prospective actions are good business.

That the Commonwealth chose to allow the milk processors to temporarily increase their prices in future consumer transactions does not transform basic economics into retroactive monetary damages. The increased profit, if any, that the milk processors will receive will be dictated by the market. The

Commonwealth is not paying the price increase and is not liable for either a sum certain amount or any potential shortfall. If the market cannot sustain the increased price, the milk processors will not increase their profits and will continue to operate at a loss. The effect of the Commonwealth's chosen price increase is simply to allow the milk processors to operate like any other private company and recover from past operating losses through future consumer transactions.[2]

The unique facts of this case drove the need for prospective relief that would allow the milk processors to avoid financial insolvency. A similar factual scenario is unlikely to reoccur, and therefore the petition does not present any issue of widespread application or national importance.

## II. The Court of Appeals' Decision Is A Factbound Application Of This Court's Precedent.

Petitioners' argument that the court of appeal's decision is inconsistent with this Court's precedent also depends on a mistaken factual premise. Petitioners primarily argue that the Eleventh Amendment is violated because the Commonwealth could be potentially liable for a monetary judgment. Pet. at 17-18. The court of appeals, however,

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[2] Put another way, imagine a situation in which the State of Texas unconstitutionally took property worth $1 million from a widget manufacturer. The Eleventh Amendment may prohibit the company from recovering $1 million in damages from Texas, but it does not prohibit the company from increasing the price of widgets to recoup the $1 million it lost from Texas's actions.

rejected that contention, and Judge Torruella specifically explained that any such argument is "pure speculation" based on the current record. Pet App. 52a (Torruella, J., concurring in the denial of rehearing en banc). Petitioners' challenge to the court of appeals' factual assumptions—particularly at this interlocutory stage—does not provide grounds for granting the petition. *NLRB* v. *Hendricks County Rural Elec. Mbrshp. Corp.*, 454 U.S. 170, 176 n.8 (1981).

1. Although the Eleventh Amendment prohibits citizen suits against a State in federal courts for monetary damages, *Edelman* v. *Jordan*, 415 U.S. 651, 663 (1974), citizens may sue state officials in their official capacity to compel compliance with federal law. *Ex parte Young*, 209 U.S. 123 (1908). Even though a State is not named a party to the action, when the action "is in essence one for the recovery of money from the state, the state is the real, substantial party in interest and is entitled to invoke its sovereign immunity from suit even though individual officials are nominal defendants." *Edelman*, 415 U.S. at 663 (quotation marks and citation omitted). "Thus the rule has evolved that a suit by private parties seeking to impose a liability which must be paid from public funds in the state treasury is barred by the Eleventh Amendment." *Id.*; *see also Regents of the Univ. of Cal.* v. *Doe*, 519 U.S. 425, 429 (1997).

In deciding whether an action is against the State for purposes of the Eleventh Amendment, this Court looks to whether state funds would satisfy the judgment. In *Hess* v. *Port Authority Trans-Hudson Corp.*, 513 U.S. 30 (1994), the Court explained "the

impetus for the Eleventh Amendment [is] the prevention of federal-court judgments that must be paid out of a State's treasury." 513 U.S. at 48. Accordingly, the Court endorsed the analysis by the "vast majority of Circuits," whereby "the state treasury factor is the most important factor to be considered . . . and, in practice, [the courts] have generally accorded this factor dispositive weight." *Id.* at 49 (quotation marks and citation omitted).

The relevant question is not whether the funds actually are paid out of the state treasury, but whether the state treasury is liable or potentially liable for the payment. In *Regents of the University of California* v. *Doe*, *supra*, the Court held that monetary relief was barred against the State even though a third party would pay the damages pursuant to an indemnification agreement. The Court held that Eleventh Amendment immunity applies "when the action is in essence one for the recovery of money from the state," and thus depends on "whether a money judgment . . . would be enforceable against the State." *Doe*, 519 U.S. at 429, 430 (quotation marks and citation omitted). According to the Court, "[t]he Eleventh Amendment protects the State from the risk of adverse judgments." *Id.* at 431.

2. The court of appeals followed this Court's precedent in its decision. The court correctly held that the Eleventh Amendment was not implicated because "the money in question would come directly from consumers of milk in Puerto Rico. . . . [I]t would be neither collected by government entities nor retained in [Puerto Rico's] treasury." Pet. App. 26a. The remedy "would, in no way, reach the coffers of

the Commonwealth." *Id.* In short, the court of appeals' decision is consistent with *Edelman*, *Hess*, and *Doe*.[3]

Petitioners primarily dispute the court's characterization of the underlying facts. Like Chief Judge Lynch, petitioners contend that the court erred because, they hypothesize, the Commonwealth could be liable for any shortfall from the price increase, and the state treasury could be implicated. Pet. at 16-17; Pet. App. 64a (Lynch, C.J., dissenting from the denial of rehearing en banc).

But, the court of appeals expressly rejected petitioners' mistaken factual assumptions. As Judge Torruella explained in his concurrence to the denial of rehearing en banc, "*the Defendants have not argued on appeal that the monies raised by the regulatory accrual are public in nature.*" *Id.* at 49a (emphasis in original). And, there is no dispute that at least some of the money has never even been in

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[3] Petitioners argue that *Hess* is inapposite because it considered whether an entity is an arm of the State, not whether a state official can assert the Eleventh Amendment. But, petitioners miss the point, as this Court indicated in *Doe*, the two issues are substantively identical. *Doe*, 519 U.S. at 431. The question in either context is whether a lawsuit puts the State at risk of an adverse money judgment and therefore raises an Eleventh Amendment concern. *Id.* Where there is no risk of an adverse judgment against the State, as the First Circuit held was the case here, the Eleventh Amendment is not implicated. Pet. App. 26a. Furthermore, petitioners themselves seem to concede the relevancy of the analysis, as they proffer an arm of the State case, *Ernst* v. *Rising*, in support of their purported circuit split. Pet. at 12-13, *see also Ernst* v. *Rising*, 427 F.3d 351 (6th Cir. 2005) (applying a factor-based test in assessing whether a government retirement system constituted an arm of the State).

petitioners' possession or control.[4] Pet at 4. Moreover, as Judge Torruella explained, "*[n]either the Commonwealth nor ORIL have been adjudged responsible for contributing funds to the special account*," and "it is pure speculation to state that the Commonwealth is legally, practically or potentially" liable to the milk producers. Pet. App. 49a, 52a (Torruella, J., concurring in the denial of rehearing en banc) (emphasis in original). The court of appeals understood and correctly applied the law. If state funds were at risk or if the Commonwealth were potentially liable, the court would have decided the case differently.

Petitioners do not point to *any* precedent in which the Court has held that the Eleventh Amendment prohibits meaningful injunctive relief against state officials that does not potentially implicate payment from state funds. *See* Pet. at 10-15. To be sure, each of their cited cases involve funds administered by state benefit programs That is to be expected, as the potential liability of the state fisc is the primary factor to consider in determining the Eleventh Amendment's applicability.

Petitioners thus have only shown a potential, hypothetical dispute as to how the preliminary injunction might be carried out. They have not shown that state funds are ultimately at risk. There is no reason for this Court to grant the petition on an incomplete interlocutory record unsupported by determinative factual findings.

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[4] As noted *supra*, the milk processors currently retain control over the money collected from consumers under the price increase.

## III. The Circuit Courts Are Not Split On The Question Presented.

Petitioners' suggestion of a circuit split fares no better. Petitioners contend that the circuits are divided on whether a court may "order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury." Pet. at i, 10-15. Not one of petitioners' cited cases, however, actually addresses that question.

In each of petitioners' cases, a plaintiff sued the State, an arm of the State, or a state officer in his or her official capacity; alleged past injury from the wrongful withholding of government benefits; and sought an order directing the specific payment of state funds collected *ex ante*. Success in each case would have necessarily entailed a monetary judgment against the State for retroactive compensatory damages. The courts of appeals therefore held that the Eleventh Amendment barred these actions. *See Esparza* v. *Valdez*, 862 F.2d 788, 795 (10th Cir. 1988) (holding that the Eleventh Amendment precluded a "judgment for past damages" that ran "against the state"); *Paschal* v. *Jackson*, 936 F.2d 940, 945 (7th Cir. 1991) ("[I]n the end, any damage award is against the state."); *Fla. Ass'n of Rehab. Facilities, Inc.* v. *Fla. Dep't of Health & Rehab. Servs.*, 225 F.3d 1208, 1221 (11th Cir. 2000) ("The district court judgment in this case effectively requires Defendants to . . pay[] Plaintiffs . . . out of the state treasury."); *see also Ernst* v. *Rising*, 427 F.3d 351, 362 (6th Cir. 2005) (holding "the state treasury would be subject to 'potential

legal liability' . . . to cover the judgment" (citation omitted)).[5]

Those decisions are unremarkable, consistent with this Court's precedent, and consistent with the court of appeals' decision in this case. As explained *supra*, the Eleventh Amendment protects the State against the risk of monetary damages paid by the state fisc. *See, e.g.*, *Hess*, 513 U.S. at 48; *Doe*, 519 U.S. at 431. Here, Puerto Rico *is not* "legally, practically or potentially" liable for paying any funds. Pet. App. 52a (Torruella, J., concurring in the denial of rehearing en banc). The court of appeals expressly held that the money is *not* state money under the unique circumstances of this case. *Id.* 26a. As Judge Torruella explained, the petitioners never even argued that the funds were public, *id.* at 49a, and petitioners cannot now contend otherwise. *California* v. *Taylor*, 353 U.S. 553, 556 n.2 (1957) (declining to recognize contentions not raised in the court of appeals). Accordingly, the court of appeals' decision is based on the facts of the case and does not create a split of authority on the law.[6]

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[5] Plaintiffs also cite *Cronen* v *Tex. Dep't of Human Servs*, 977 F 2d 934 (5th Cir 1992), which does not implicate the Question Presented, nor petitioners' purported circuit split There, the court decided only that *Ex parte Young* does not allow a citizen to sue a "state *qua* state" for either monetary damages or injunctive relief *Id* at 938

[6] To the extent any split exists regarding whether the Eleventh Amendment is implicated where a third party will pay the judgment, as petitioners admit, that split was resolved by *Doe* and is now stale Pet at 13 (stating that no court had ordered "retrospective monetary relief against a sovereign since this Court's decision in *Doe*")

## IV. This Case Is A Poor Vehicle For Deciding The Question Presented.

Finally, the interlocutory nature of the case and the complex threshold legal issues that must precede a determination on the merits make this case an exceedingly poor vehicle for review at this time.

1. The court of appeals' decision affirms a preliminary injunction issued to stabilize the milk industry and prevent the milk processors from going bankrupt pending adjudication of their claims. No final ruling on the merits has been made. Nor has the district court issued a permanent injunction.

Because of the interlocutory nature of the case, a great deal of confusion regarding the scope of the district court's injunction and the nature of the funds exists. The proposed regulation that would permit petitioners to assert control over the money in question has not been implemented, further complicating any analysis of the Eleventh Amendment implications. As Judge Torruella explained, at this point, it is "pure speculation" as to how this injunction will actually work in practice, and petitioners failed to provide any details of the "temporary mechanism" they unilaterally designed and adopted. Pet. App. 49a n.2, 52a. In addition, petitioners did not argue or build the record on appeal that the monies at issue are public funds. *Id.* at 49a. Accordingly, even if the Court were interested in addressing the factual arguments regarding the nature of the funds and the

Commonwealth's potential liability, the record is devoid of the necessary facts to do so.[7]

2. The petition also presents significant novel and difficult legal questions that would complicate the Court's resolution of the Question Presented.

a. As an initial matter, this Court has not decided that the Eleventh Amendment applies to Puerto Rico. By its terms, the Eleventh Amendment protects against lawsuits "commenced or prosecuted against one of the United States," and makes no reference to United States Territories or "sovereigns." U.S. CONST. AMEND. XI. At least two former justices, accordingly, have suggested that the Eleventh Amendment does not apply to unincorporated Territories such as Puerto Rico. *See Ngiraingas* v. *Sanchez*, 495 U.S. 182, 205 (1990) (Brennan, J., dissenting) ("[A]n unincorporated Territory . . . can have no immunity against a claim like the one here—a suit in federal court based on federal law."); *Balzac* v. *Porto Rico*, 258 U.S. 298, 305-07 (1922) (concluding that Puerto Rico is an unincorporated Territory). Because the parties have assumed that the Eleventh Amendment applies to Puerto Rico, the issue was not briefed nor addressed in the lower courts.

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[7] Following the district court's final disposition of the case, petitioners will be able to raise their current claims—together with any other claims that may arise as a result of the additional proceedings on remand—in a single petition for a writ of certiorari. *See Major League Baseball Players Ass'n* v. *Garvey*, 532 U.S. 504, 508 n.1 (2001) (per curiam) (stating that this Court "ha[s] authority to consider questions determined in earlier stages of the litigation where certiorari is sought from" the most recent judgment).

While the Court has assumed Puerto Rico to be protected by the Eleventh Amendment in a previous case, *see Puerto Rico Aqueduct & Sewer Auth.* v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 n.1 (1993) ("[E]xpress[ing] no view on this matter."), such a procedural posture certainly is not preferable. To be sure, such an assumption would purposefully avoid the potentially dispositive threshold legal issue—if the Eleventh Amendment does not apply, the entire exercise has been for naught—but yet the record in this case has not been developed so that resolution of the ultimate question is appropriate. *See Ticor Title Ins. Co.* v. *Brown*, 511 U.S. 117, 118 (1994) (dismissing as improvidently granted a writ of certiorari that would "require us to resolve a constitutional question that may be entirely hypothetical").

b. Further complicating matters, the district court's preliminary injunction was issued to remedy a Takings claim. There is currently an open question as to whether the Eleventh Amendment bars retroactive monetary compensation by the State for Takings claims. As this Court recognized in *First English Evangelical Lutheran Church of Glendale* v. *County of Los Angeles*, 482 U.S. 304, 316 & n.9 (1987), "the Constitution . . . dictates the remedy for interference with property rights amounting to a taking" and, therefore, notwithstanding claims of immunity, retroactive monetary relief may be "required by the Constitution." This Court could not cleanly resolve the Question Presented without first addressing whether or not the Takings Clause abrogates Eleventh Amendment immunity. Even if the Court were interested in the Question Presented, a case that did not present this complicated

threshold legal question would be a much better vehicle.

c. Lastly, petitioners' arguments presume that the district court's relief is retroactive. The court of appeals, however, did not address that question but merely assumed it to be the case. And, that question is far from simple

The line between prospective and retroactive relief is not always distinct. *Hutto* v. *Finney*, 437 U.S. 678, 690 (1978) (citing *Edelman*, 415 U.S. at 667). This Court, thus, has held that an award of attorney's fees for past work is not retroactive. *Id.*; *see also Missouri* v. *Jenkins*, 491 U.S. 274, 284 (1989) ("[T]he Eleventh Amendment has no application to an award of attorney's fees, ancillary to a grant of prospective relief, against a State."). While these fees appeared to be retroactive in the sense that they were to compensate the plaintiff for work performed prior to the judgment, the Court held that the fees were "ancillary" to the prospective relief otherwise available and therefore permissible. *Hutto*, 437 U.S. at 690-93; *see also Quern* v. *Jordan*, 440 U.S. 332, 349 (1979) (injunction to notify class members that their federal suit is at an end and that they may wish to pursue existing state administrative procedures is "ancillary" to prospective relief already ordered).

Likewise, compensatory relief that is necessary to ensure meaningful prospective relief is not considered to be retroactive. The Court has held that an order requiring a State to pay for remedial educational programs designed to ensure that segregated students would be able to catch up to their peers "fit[] squarely within the prospective-

compliance exception" announced in *Ex parte Young*. *Milliken* v. *Bradley*, 433 U.S. 267, 289 (1977). As the Court explained, while the court could prospectively end the unconstitutional inequality through "judicial fiat," that would not "wipe the slate clean by one bold stroke." *Id.* at 290. Injuries from the antecedent violations would continue absent some additional action. Thus, even though the remedial educational programs were "'compensatory' in nature . . . they [we]re part of a plan that operates prospectively to bring about the delayed benefits of a unitary school system" and therefore not barred by the Eleventh Amendment. *Id.*

Here, the Commonwealth's chosen price increase operates prospectively on future consumer transactions. The purpose of the injunction is to ensure that the milk processors do not go bankrupt from their past losses and to stabilize the milk industry. At a minimum, strong arguments exist that such relief is prospective because it is necessary to ensure effective relief or is at least ancillary to the remaining undisputed prospective relief. After all, like the ongoing effect of the constitutional violation in *Milliken*, the threat of bankruptcy is not eliminated simply because sometime in the future the milk processors will be allowed to make a profit. The distinction between prospective and retrospective relief is already murky, and for the Court either to assume the nature of the relief or to attempt to resolve it on an incomplete record merely risks engendering further confusion.

In sum, even if the petitioners were correct that the First Circuit's opinion will "'effectively eliminate the constitutional immunity' of Puerto Rico and

other sovereigns," Pet. at 20, surely a better vehicle in which to address the Question Presented will arise.

## CONCLUSION

For all of the foregoing reasons, the Court should deny the petition for a writ of certiorari.

Respectfully submitted,

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No. 10-74

# In the Supreme Court of the United States

JAVIER RIVERA AQUINO, SECRETARY,
PUERTO RICO DEPARTMENT OF AGRICULTURE,
ET AL., PETITIONERS

*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## SUPPLEMENTAL BRIEF FOR THE PETITIONERS

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*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## SUPPLEMENTAL BRIEF FOR THE PETITIONERS

The federal government's position in this case is thoroughly mystifying. The government primarily contends that this Court's review is unnecessary because the court of appeals reached the right result in refusing to afford sovereign immunity. Specifically, the government asserts that the relief ordered by the district court, while requiring the Commonwealth of Puerto Rico to compensate respondents for past constitutional injuries, was not monetary. That will come as news to the people of Puerto Rico, who, as a result of the district court's order, have been paying an extra 1.5¢ on every quart of milk they buy. But more fundamentally, the government's position, like the court of appeals' decision, cannot be recon-

ciled with the settled principle that the relevant inquiry for purposes of sovereign immunity is whether liability would ultimately fall on the sovereign—not whether the sovereign would be the ultimate source of the funds used to satisfy that liability. Although the government also reiterates some of the vehicle arguments made by respondents, those arguments—which the Court presumably considered before it called for the government's views—are as meritless now as when they were initially raised.

Given the obvious flaws in the government's arguments, one is left with the sense that the government does not want the Court to grant review in this case, but without a good sense of the reasons why. As the amicus participation of a majority of the States reflects, the court of appeals' decision presents an exceptionally important constitutional issue—and, if that decision is allowed to stand, it will open up a dangerous loophole in the doctrine of sovereign immunity, by allowing a plaintiff to seek relief previously understood to be foreclosed by sovereign immunity under the guise of an *Ex parte Young* action. The decision below is inconsistent with decisions both of this Court and of other circuits. That inconsistency warrants further review and correction.

### A. The Court Of Appeals' Decision Conflicts With The Decisions Of This Court And Other Circuits

1. a. The federal government does not directly defend the court of appeals' holding that a federal court can order retrospective relief in an action under *Ex parte Young*, 209 U.S. 123 (1908), as long as the necessary funds do not come directly from the general treasury. See Pet. App. 25a-26a. Indeed, the government conspicuously does not argue that a court could directly impose the mechanism that the Commonwealth adopted to

comply with the district court's order: namely, the 1.5¢ surcharge on every quart of milk sold in Puerto Rico. Instead, the government contends (Br. 6-10) that the relief ordered by the district court was not monetary relief for purposes of *Ex parte Young* because the Commonwealth *could* have complied with the order by taking some other action to raise the necessary money: for example, by adopting a regulation raising the maximum price that processors were allowed to charge for milk.

To state that contention is to refute it. As this Court has repeatedly explained, the exception carved out in *Ex parte Young* for suits against officials does not extend to claims for "[r]elief that in essence serves to compensate a party injured in the past." *Papasan* v. *Allain*, 478 U.S. 265, 278 (1986). It is undisputed that the district court ordered the Commonwealth to provide compensation, in the form of money, for respondents' past constitutional injuries—and the government does not suggest otherwise. See Pet. App. 197a. Admittedly, the district court did not order the Commonwealth to come up with the funds through any particular means, but instead allowed it to raise the funds "through * * * any * * * available mechanism of its choosing." *Ibid.* But regardless of the ultimate source of the funds, the relief that was ordered was monetary by any definition, because the Commonwealth was required to take action to generate money that would be used to compensate respondents.

Indeed, money not only is already being collected from Puerto Rico consumers, but is being directly retained by respondents themselves. See Pet. 4.[1] Given

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[1] As the government notes (Br. 15-16), the parties have disputed whether the money should instead be held in a segregated account by the Milk Industry Development Fund. Neither the government

that money is actually changing hands as a result of the district court's order, it blinks reality to conceive of the relief as anything but monetary. Even the court of appeals recognized as much when it noted that, under the Commonwealth's chosen mechanism, "the *money* in question would come directly from consumers of milk in Puerto Rico." Pet. App. 26a (emphasis added).

Crucially, the federal government does not dispute that, no matter what mechanism it chose for complying with the district court's order, the Commonwealth would ultimately be responsible if the chosen mechanism raised insufficient funds to compensate respondents for its past constitutional violations. If, for example, the Commonwealth raised the maximum price that processors were allowed to charge but milk sales actually fell as a result, the Commonwealth would be on the hook for any ensuing shortfall. See Pet. App. 64a (Lynch, C.J., dissenting from denial of rehearing en banc).

Under this Court's sovereign-immunity jurisprudence, that is the beginning and end of the inquiry. Most notably, in *Regents of University of California* v. *Doe*, 519 U.S. 425 (1997), the Court unanimously held that, for purposes of sovereign immunity, "it is the [sovereign] entity's potential legal liability * * * that is relevant"—not the source of the funds used to satisfy the liability. *Id.* at 431. That principle, in turn, is rooted in the broader principle that sovereign immunity protects against "the indignity of subjecting a [sovereign] to the coercive process of judicial tribunals at the instance of private parties." *Puerto Rico Aqueduct & Sewer Auth.*

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nor any of the parties, however, has taken the position that whether the money is so held is material to the sovereign-immunity analysis.

v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 146 (1993) (citation omitted).

Although *Doe* was the most-cited case in the petition for certiorari (and the principal authority on which Chief Judge Lynch relied in dissent below), *the federal government does not so much as cite it, let alone distinguish it, in its brief to this Court.* That would be remarkable enough in a brief filed by a private litigant. But in a brief filed by the Solicitor General, it is simply astounding. And it is all the more astounding because the government participated in *Doe* as an amicus curiae *on the side of the entity seeking immunity.* See Oral Arg. Tr. at 18-19, 20, *Doe*, *supra* (Dec. 2, 1996) (argument of Assistant to the Solicitor General Blatt) (contending that, "as a State entity[,] * * * it is the university who is subject to the coercive enforcement powers of the court," "is the party against whom judgment is sought," and "is on the hook for the judgment"). The government disrespects the Court when it fails to explain how its position here can be reconciled either with its own position in *Doe* or, more importantly, with the Court's unanimous reasoning in that case.

In the portion of its brief arguing that the relief ordered by the district court was not monetary (Br. 6-9), the only case the government cites is *Ex parte Young* itself. But *Ex parte Young* is readily distinguishable, because it involved "a suit against state officials * * * to enjoin enforcement of a railroad commission's order requiring a reduction in rates." *Verizon Md. Inc.* v. *Public Service Comm'n*, 535 U.S. 635, 646 (2002). Unlike respondents here, the plaintiffs in *Ex parte Young* did not seek an order requiring any state actor to compensate them for a past violation. Permitting relief of the type respondents are seeking would entirely erode the distinction between suits permitted by *Ex parte Young* and

suits barred by sovereign immunity—and would thereby "effectively eliminate the constitutional immunity of the States." *Pennhurst State Sch. & Hosp.* v. *Halderman*, 465 U.S. 89, 105 (1984).

b. The federal government alternatively suggests (Br. 12), but stops short of affirmatively arguing, that the relief at issue here is permissible in an *Ex parte Young* action because it is prospective. For purposes of *Ex parte Young*, however, relief is impermissibly retrospective whenever it would compensate a plaintiff for a past violation. See, *e.g.*, *Papasan*, 478 U.S. at 278. And it could not be clearer that that is what the district court awarded. See Pet. App. 197a.

The government hints (Br. 12) that the analysis may operate differently in the ratemaking context. To be sure, in that context, it is possible to imagine a situation in which it is difficult to disaggregate the prospective and retrospective components of court-ordered relief. In this case, however, there is no such difficulty, because the district court ordered bifurcated relief that neatly tracks the distinction between permissible prospective and impermissible retrospective relief: revisions to the regulatory regime, which will allow respondents to recover a higher rate of return going forward, and the relief at issue here, which enables respondents to recover for constitutional violations dating back to 2003 until the revised regulatory regime takes effect. See Pet. App. 197a. By its terms, the latter relief is retrospective, because it seeks to compensate respondents for past violations.[2]

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[2] Because the prospective relief was designed to be sufficient on its own to remedy any ongoing constitutional violation, the retrospective relief cannot plausibly be viewed as a "necessary step[]" in

Relying on *Green* v. *Mansour*, 474 U.S. 64 (1985), the government further contends (Br. 11) that retrospective *non-monetary* relief is available in an *Ex parte Young* action. Of course, that contention is relevant only if the relief at issue here is correctly characterized as non-monetary—but it is in any event meritless. In *Green*, the Court rejected the plaintiffs' claims not only for retrospective declaratory relief against a state official, but also for retrospective "notice relief," on the ground that such relief "is not the type of remedy designed to prevent ongoing violations of federal law" and therefore could not be "order[ed] * * * as an independent form of relief." 474 U.S. at 71. And since *Green*, the Court has consistently taken the position that "the exception [of *Ex parte Young*] * * * applies only to prospective relief [and] does not permit judgments against state officers declaring that they violated federal law in the past." *Metcalf & Eddy*, 506 U.S. at 146; cf. *Verizon*, 535 U.S. at 645 (permitting claim for declaratory as well as injunctive relief where "no past liability of the State * * * is at issue").

2. The federal government contends that this case does not implicate a circuit conflict on the ground that "petitioners can comply with the district court's order without using any commonwealth funds." Br. 13. In so contending, however, the government misapprehends the nature of the circuit conflict. Numerous courts of appeals have held, both before and after this Court's decision in *Doe*, that the defense of sovereign immunity is available whenever a plaintiff is seeking retrospective relief that is monetary in nature, regardless of the source

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the implementation of the prospective relief. *Milliken* v. *Bradley*, 433 U.S. 267, 290 (1977).

of the funds used to provide that relief. See Pet. 10-15. In fact, since the government filed its brief, the District of Columbia Circuit has acknowledged the very conflict identified in the petition. See *Greater New Orleans Fair Housing Action Center* v. *HUD*, Nos. 10-5257 & 10-5269, 2011 WL 1327713, at *4 (Apr. 8, 2011). That acknowledgment confirms the existence of a live circuit conflict warranting the Court's review.

3. In our view, the court of appeals' decision is so out of step with this Court's sovereign-immunity precedents, and with the unbroken line of lower-court authority since *Doe*, that summary reversal would be appropriate. But at a minimum, the federal government's position reflects lingering confusion on the scope of sovereign immunity and thus illustrates the need for plenary review. If it is allowed to stand, the court of appeals' decision will serve as a template for a plaintiff who wishes to seek retrospective monetary relief from a sovereign; such a plaintiff will be able to do so through the simple expedient of bringing an *Ex parte Young* action and structuring his request for relief so that the requisite funds come (or could conceivably come) from a source other than the sovereign's treasury. See Pet. App. 63a (Lynch, C.J., dissenting from denial of rehearing en banc). It is for that reason that the court of appeals' decision is so troubling not only to the Commonwealth of Puerto Rico, but also to the twenty-six States that are supporting the petition for certiorari.[3] As Chief Judge Lynch noted, the "serious issues" presented by this case "deserve [the] attention" of the Court. *Id.* at 54a, 56a.

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[3] By contrast, the decision below is of only limited importance to the federal government in light of the broad statutory waivers of its immunity. See, *e.g.*, 28 U.S.C. 1346(b), 1491.

### B. This Case Is An Optimal Vehicle For Consideration Of The Question Presented

The federal government also contends (Br. 13-17) that this case would be an inappropriate vehicle for consideration of the question presented. For the most part, the reasons it cites are duplicative of those identified by respondents, which have already been addressed in petitioners' reply brief. Only two points warrant additional response.

1. In the span of just six pages, the government argues both that petitioners are raising the sovereign-immunity issue too late (because they did not appeal from the denial of their motion to dismiss) and that petitioners are raising the issue too early (because they could raise it after the district court enters final judgment). See Br. 10, 13-16. The obvious inconsistency between those arguments is a sufficient basis for rejecting them out of hand. But each argument also lacks merit on its own terms.

As to the argument that petitioners are raising the sovereign-immunity issue too late: assuming that petitioners could have taken an appeal as of right at the motion-to-dismiss stage, petitioners' failure to do so was entirely understandable. In rejecting their sovereign-immunity objection, the district court reassured petitioners that respondents were merely "seeking a prospective injunctive relief" and were "not seeking damages nor a monetary compensation." Pet. App. 214a. It was only after the district court held the Commonwealth liable for past violations, and ordered it to come up with funds to cover that liability, that it became clear that respondents' claim for retrospective monetary liability remained alive. See Second Am. Compl. ¶ 92, at 39. Petitioners have diligently litigated the sovereign-immunity issue ever since.

As to the argument that petitioners are raising the sovereign-immunity issue too early: there is no valid reason why the Commonwealth should have to wait until final judgment before taking an appeal on that issue. In permitting interlocutory appeals from rulings on sovereign immunity, this Court explained that the benefit of sovereign immunity would be lost if a defendant could not invoke it until after trial. See *Metcalf & Eddy*, 506 U.S. at 143-144. And the argument that the Commonwealth should have to wait until final judgment is a bit rich coming from the federal government, which has raised sovereign-immunity objections at every conceivable stage of litigation—including the preliminary-injunction stage. See, *e.g.*, *United States* v. *Bedford Associates*, 618 F.2d 904, 913 (2d Cir. 1980).

The government suggests (Br. 15-16) that further review would be premature in this case because the ongoing proceedings below could affect the analysis on the question presented. In the order under review, however, the district court definitively held that respondents had suffered past and ongoing constitutional violations, see Pet. App. 192a, and ordered the Commonwealth to come up with funds to compensate respondents for those past violations, see *id.* at 197a. By contrast, the ongoing proceedings in the district court (and an interlocutory appeal recently noticed by petitioners) are focused on the details of how to calculate the rate of return to which respondents will be entitled. See, *e.g.*, Opinion and Order, Dist. Ct. Dkt. No. 1804 (Jan. 3, 2011); Notice of Appeal, Dist. Ct. Dkt. No. 1868 (Feb. 2, 2011). Because the relief at issue here is in all relevant respects final and has in fact been implemented, the mere fact that proceedings are ongoing in the same case should not deter this Court's review.

2. Finally, the federal government contends (Br. 16-17) that the Court should deny review because it has not yet squarely held that Puerto Rico is entitled to sovereign immunity. The Court, however, can decide this case on the assumption that Puerto Rico is entitled to sovereign immunity—regardless of whether, as the government notes, "this case presents a substantive question of the scope of immunity." Br. 16. Like respondents, moreover, the government does not affirmatively dispute that Puerto Rico is entitled to sovereign immunity; to the contrary, the government hints that it is. See Br. 17.

To the extent that there is any residuum of uncertainty concerning Puerto Rico's entitlement to sovereign immunity, this Court could readily direct the parties to address that issue in their merits briefing. But however the Court chooses to proceed at the merits stage, it should not penalize the Commonwealth of Puerto Rico by relying on that residuum of uncertainty as a basis for denying certiorari where, as here, the Commonwealth seeks the Court's review on a generally applicable question concerning the scope of sovereign immunity. There can be no dispute that the question presented in this case is a substantial one of exceptional importance not only to Puerto Rico, but also to a majority of the States. To deny review simply because this case arises from Puerto Rico would not only leave the First Circuit's erroneous and far-reaching decision in place; it would work an affront to the Commonwealth and its people.

* * * * *

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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No. 10-74

# In the Supreme Court of the United States

JAVIER RIVERA AQUINO, SECRETARY, PUERTO RICO DEPARTMENT OF AGRICULTURE, ET AL., PETITIONERS

*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## REPLY BRIEF FOR THE PETITIONERS

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*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## REPLY BRIEF FOR THE PETITIONERS

After reading respondents' briefs in opposition, one could be forgiven for forgetting what the First Circuit actually held in this case. It held that a federal court could order retrospective monetary relief against a sovereign as long as the necessary funds do not come directly from the general treasury. The First Circuit's decision conflicts with the decisions of this Court and numerous other circuits, and it is of exceptional importance to the Commonwealth of Puerto Rico and other sovereigns. It was for those reasons that Chief Judge Lynch stated that this case presents "serious issues" that "deserve [the] attention" of the Court. And it was for those reasons that twenty-six States have filed an amicus brief

asking this Court not only to grant review, but summarily to reverse the judgment below.

Respondents offer conspicuously little by way of a defense of the First Circuit's actual holding. Instead, they identify three potential vehicle problems that they claim justify the denial of further review. None of those issues, however, presented an obstacle to the First Circuit's reaching the holding it did, and none presents an obstacle to this Court's review either. Put simply, the First Circuit's decision cries out for further review and correction.

### A. The Court Of Appeals' Decision Conflicts With The Decisions Of This Court And Other Circuits

1. As explained in the petition, this Court has repeatedly held that the exception to the principle of sovereign immunity first recognized in *Ex parte Young*, 209 U.S. 123 (1908), is available only where a plaintiff seeks prospective, rather than retrospective, relief. See, *e.g.*, *Verizon Md. Inc.* v. *Public Service Comm'n*, 535 U.S. 635, 645 (2002). This Court has also repeatedly held that, in determining whether the defense of sovereign immunity is available where the plaintiff is seeking retrospective monetary relief, a court should not consider whether the relief would take funds directly from the general treasury; instead, the relevant inquiry is whether liability would ultimately fall on the sovereign. See, *e.g.*, *Regents of Univ. of Cal.* v. *Doe*, 519 U.S. 425, 431 (1997). Accordingly, numerous courts of appeals have held that, regardless of the potential effect on the general treasury, sovereign immunity bars any suit in which the plaintiff is seeking retrospective monetary relief from the sovereign. See Pet. 10-13.

2. Respondents do not meaningfully dispute any of those propositions. Instead, they contend that the deci-

sion below gives rise to no valid conflict because the district court ordered "prospective injunctive relief," Vaquería Br. 13, and because the Commonwealth bears "no * * * potential monetary liability," Suiza Br. 11. That contention is flawed in every particular.

a. As a preliminary matter, the court of appeals in this case unambiguously concluded that it was *irrelevant* to the sovereign-immunity analysis whether the relief the district court ordered was prospective or retrospective. See Pet. App. 24a. Instead, it proceeded to hold that a federal court could order even retrospective relief against a sovereign as long as the necessary funds do not come directly from the general treasury. See *id.* at 25a-26a. It is that holding which cannot be reconciled with the decisions of this Court or other circuits and which, if allowed to stand, will have enormous consequences for Puerto Rico and other sovereigns.

b. Respondents seemingly suggest that the court of appeals' holding was simply unnecessary because the relief ordered was prospective. To begin with, in light of the court of appeals' plainly erroneous holding, if this Court were to conclude that there is any ambiguity as to whether the relief ordered was prospective or retrospective, it should vacate the judgment below and remand for the court of appeals to consider that issue in the first instance.

But in any event, there can be no doubt that the relief which the plaintiffs in this case were seeking, and which the district court ordered, was retrospective. In their complaint, respondents unambiguously sought to "*recover the losses they have experienced* on account of the unconstitutional acts and decisions herein under attack." Second Am. Compl. ¶ 92, at 39 (emphasis added). Notably, respondents do not disavow that claim in their briefs before this Court. In and of itself, the existence of that

claim is sufficient to trigger the Commonwealth's sovereign immunity. See pp. 6-7, *infra*.

The district court, moreover, did not simply allow respondents to recover a higher rate of return going forward, but also ordered ORIL to provide compensation for respondents' "deficient rate of return" starting from the beginning of 2003 (*i.e.*, more than eighteen months before respondents filed suit). Pet. App. 21a, 197a. The latter relief is retrospective by any measure, because, consistent with what respondents were seeking in their complaint, it would compensate them for a past violation of federal law. See *Papasan* v. *Allain*, 478 U.S. 265, 278 (1986). Although respondents contend (Vaquería Br. 1; Suiza Br. 12-13) that the *purpose* of the relief was to enable them to rebuild their capital bases, the district court did not specifically state that it was ordering the relief for that purpose, see Pet. App. 197a; even if it had, the relief would not be prospective, because the relief would still be redressing a *past* violation, see *id.* at 60a & n.8 (Lynch, C.J., dissenting from denial of rehearing en banc);[1] and, in holding that the Commonwealth was not entitled to sovereign immunity, the court of appeals expressly declined to accept respondents' contention, see *id.* at 24a.

c. There can also be no doubt that the plaintiffs in this case were seeking to impose, and the district court actually did impose, monetary liability on the Commonwealth. As noted above, respondents sued petitioners, in their capacities as officials of the Commonwealth, in order to "recover the losses they have experienced on ac-

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[1] Indeed, respondent Vaquería acknowledges as much. See Br. 26 (noting that "the purpose of the injunction is to ensure that [respondents] do not go bankrupt *from their past losses*") (emphasis added).

count" of the alleged constitutional violations. Second Am. Compl. ¶ 92, at 39. Simply by virtue of the fact that respondents were *seeking* a court order awarding monetary relief against the Commonwealth for past constitutional violations, this case implicates the Commonwealth's sovereign immunity. See pp. 6-7, *infra*.

The district court, moreover, ordered ORIL to adopt a mechanism that would allow respondents to recover monetary damages for the Commonwealth's past constitutional violations. See Pet. App. 197a. It is irrelevant that, as respondents repeatedly note (Vaquería Br. 9, 13; Suiza Br. 14-15), the court did not specifically order the Commonwealth to pay "public" funds directly out of the general treasury or to raise the funds through a particular means (such as a tax), but instead allowed the Commonwealth to raise the funds "through * * * any * * * available mechanism of [its] choosing." Pet. App. 197a.[2] For sovereign-immunity purposes, the key fact is that respondents were seeking to impose, and the district court actually did impose, monetary liability on the Commonwealth—as is vividly illustrated by the fact that, by their own admission, respondents are already retaining money collected from the 1.5¢ surcharge on milk sales that the Commonwealth adopted to comply the district court's order. See Vaquería Br. 10, 12 n.1, 19 n.4.

This Court should not be distracted by respondents' efforts to introduce factual complexity where there is none. Because the court of appeals' actual holding cannot be reconciled with the decisions of this Court or oth-

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[2] It is therefore also irrelevant that, as respondents note (Vaquería Br. 2, 11, 18, 21, 22; Suiza Br. 11), petitioners did not argue below, in so many words, that the raised funds were "public in nature."

er circuits, the Court should either grant plenary review or reverse outright.

### B. This Case Is An Optimal Vehicle For Consideration Of The Question Presented

Respondents identify three potential reasons why this case would be a poor vehicle for consideration of the question presented. Those reasons are both individually and collectively insubstantial.

1. Respondents contend (Vaquería Br. 22-23; Suiza Br. 6-7) that the Court should deny review simply because this case arises in an interlocutory posture. That contention is wholly unfounded.

To be sure, as respondent Suiza notes (Br. 6-7), this Court ordinarily prefers not to grant review when cases are in an interlocutory posture. But that has not been the Court's practice with regard to cases presenting questions of immunity, including sovereign immunity. To the contrary, the Court has held that rulings on questions of sovereign immunity are immediately appealable even at the motion-to-dismiss stage, see *Puerto Rico Aqueduct & Sewer Auth.* v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 142-147 (1993), and has itself granted review on such questions at that stage, see, *e.g.*, *Seminole Tribe of Fla.* v. *Florida*, 517 U.S. 44 (1996). That is for good reason, because "[i]t is the fact that a private party is allowed to sue," not "the burden of litigation or the relief sought," that infringes sovereign immunity. *Alabama* v. *North Carolina*, 130 S. Ct. 2295, 2318 (2010) (Roberts, C.J., concurring in part and dissenting in part); see *Federal Maritime Comm'n* v. *South Carolina Ports Auth.*, 535 U.S. 743, 765 (2002). Put another way, the benefit of sovereign immunity would be entirely lost if a defendant could not invoke it until after trial. See *Metcalf & Eddy*, 506 U.S. at 143-144.

That rationale applies *a fortiori* here, where the sovereign-immunity issue comes to the Court not at the motion-to-dismiss stage, but rather at the preliminary-injunction stage. As respondents note (Vaquería Br. 8; Suiza Br. 2), the district court issued the preliminary injunction after more than fifty evidentiary hearings over three years. In doing so, moreover, the district court did not simply determine that respondents were *likely* to prevail on their constitutional claims; it definitively held that respondents had suffered past and ongoing constitutional violations. See Pet. App. 192a. Although the mere fact that respondents were *seeking* to impose monetary liability on the Commonwealth for past constitutional violations is sufficient to implicate the Commonwealth's sovereign immunity, the fact that the district court has held the Commonwealth liable, and ordered it to set aside funds to cover that liability, eliminates any doubt that further review is appropriate.[3]

2. Respondents next contend (Vaquería Br. 23-24; Suiza Br. 8-11) that the Court should deny review because it has not yet definitively held that Puerto Rico is entitled to sovereign immunity. That contention also lacks merit.

As a preliminary matter, as noted in the petition (at 7 n.1), the Court can decide this case on the assumption that Puerto Rico is entitled to sovereign immunity. The

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[3] Respondent Suiza contends (Br. 27-30) that petitioners waived the Commonwealth's immunity by participating in expert discovery after the district court rejected that defense. That is an exceedingly peculiar contention. When a district court proceeds with the case while an appeal on the immunity issue is ongoing, a sovereign is hardly required to refuse to participate in any further proceedings in the district court in order to preserve the immunity issue on appeal.

Court decided *Metcalf & Eddy* on that assumption, see 506 U.S. at 141 n.1, and there is no reason why the Court should do otherwise here. That is particularly true because respondents have not disputed the proposition that Puerto Rico is entitled to sovereign immunity at any stage of this litigation; indeed, they stop short of affirmatively disputing it even in their briefs before this Court. See Vaquería Br. 23; Suiza Br. 8.

In any event, the proposition that Puerto Rico is entitled to sovereign immunity is not open to serious debate. Since its decision in *Erzatty* v. *Puerto Rico*, 648 F.2d 770, 776 n.7 (1981) (Breyer, J.), the First Circuit has reiterated that Puerto Rico is entitled to sovereign immunity in at least twenty-seven other cases, stating some time ago that Puerto Rico's immunity is "beyond dispute." *Puerto Rico Ports Auth.* v. *M/V Manhattan Prince*, 897 F.2d 1, 9 (1st Cir. 1990). Although the issue primarily arises in the First Circuit because of its jurisdiction over Puerto Rico, other courts have concluded that Puerto Rico "enjoys the same immunity from suit possessed by the States." *E.g.*, *United States* v. *Laboy-Torres*, 553 F.3d 715, 721 (3d Cir. 2009) (O'Connor, J.).

That conclusion, moreover, is clearly correct. This Court has recognized that Puerto Rico possesses "a measure of autonomy comparable to that possessed by the States." *Examining Board of Engineers, Architects & Surveyors* v. *Flores de Otero*, 426 U.S. 572, 597 (1976). As Justice O'Connor has explained, "[l]ike the States, [Puerto Rico] has a republican form of government, organized pursuant to a constitution adopted by its people, and a bill of rights." *Laboy-Torres*, 553 F.3d at 721. And to the extent that any contrary argument relies on the approach of the Insular Cases, which held that unincorporated territories do not enjoy the full protections of the Constitution, see, *e.g.*, Vaquería Br. 23 (citing *Balzac*

v. *Porto Rico*, 258 U.S. 298 (1922)), this Court has since distanced itself from that approach. See, *e.g.*, *Boumediene* v. *Bush*, 128 S. Ct. 2229, 2255 (2008). The theoretical possibility that the Court could conclude that Puerto Rico is not entitled to sovereign immunity is thus no reason to deny review here.[4]

3. Finally, respondents contend (Vaquería Br. 24-25; Suiza Br. 21-23) that the Court should deny review because sovereign immunity does not bar a claim for retrospective monetary relief under the Takings Clause. That contention is invalid.

The courts of appeals have uniformly held that, notwithstanding the express reference in the Takings Clause to "just compensation," sovereign immunity bars a claim under the Takings Clause, like any other federal claim, for retrospective monetary relief. See, *e.g.*, *Seven Up Pete Venture* v. *Schweitzer*, 523 F.3d 948, 953-955 (9th Cir.), cert. denied, 129 S. Ct. 258 (2008); *DLX, Inc.* v. *Kentucky*, 381 F.3d 511, 526-528 (6th Cir. 2004), cert. denied, 544 U.S. 961 (2005); *John G. & Marie Stella Kenedy Memorial Foundation* v. *Mauro*, 21 F.3d 667, 674 (5th Cir.), cert. denied, 513 U.S. 1016 (1994); *Garrett* v. *Illinois*, 612 F.2d 1038, 1040 (7th Cir.), cert. denied, 449 U.S. 821 (1980).[5] Those courts have explained that "the * * * self-executing nature of the Takings Clause does not alter the conventional application of the Eleventh

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[4] Should the Court wish to put to rest any doubt concerning whether Puerto Rico is entitled to sovereign immunity, it should grant plenary review in this case and direct the parties to address that question in their merits briefing.

[5] The earlier First Circuit cases on which respondent Suiza relies (Br. 22-23) are readily distinguishable. See Pet. App. 61a n.9 (Lynch, C.J., dissenting from denial of rehearing en banc).

Amendment," noting that a plaintiff may still pursue a claim for injunctive and declaratory relief against a State in federal court and may also pursue a claim for retrospective monetary relief in state court. *Seven Up Pete Venture*, 523 F.3d at 954.

In support of the contrary argument, respondents cite a footnote in this Court's decision in *First English Evangelical Lutheran Church of Glendale* v. *County of Los Angeles*, 482 U.S. 304 (1987). As the caption suggests, however, *First English* involved a takings claim against a county, which is not entitled to sovereign immunity in federal court. See, *e.g.*, *Northern Ins. Co.* v. *Chatham County*, 547 U.S. 189, 193-194 (2006). *First English* thus presented no issue concerning the potential availability of a takings claim for retrospective monetary relief against an entity that actually possesses sovereign immunity. In any event, in the cited footnote, the Court ultimately concluded only that "it is the Constitution that dictates the remedy for interference with property rights amounting to a taking"—not that the Constitution mandates that the remedy of retrospective monetary relief be available in *federal court* against an otherwise immune sovereign. See *First English*, 482 U.S. at 316 n.9. It is therefore unsurprising that, even after *First English*, lower courts have continued consistently to hold that sovereign immunity bars takings claims for retrospective monetary relief. See, *e.g.*, *Seven Up Pete Venture*, 523 F.3d at 953-954 & n.6; *DLX*, 381 F.3d at 527-528.

In addition, contrary to respondent Vaquería's contention (Br. 24-25), the question whether sovereign immunity bars a claim for retrospective monetary relief under the Takings Clause is logically subsequent, not antecedent, to the question whether sovereign immunity is available in the first place for respondents' takings and

other claims. Just as the court of appeals did, therefore, this Court may address and resolve the question presented without reaching the Takings Clause question. In the event the Court reverses the judgment of the court of appeals, respondents would be free to advance their Takings Clause argument on remand. And should the Court conclude that the Takings Clause question is a substantial one (notwithstanding the absence of a circuit conflict) and wish to resolve it, the Court can readily do so in this case in the course of plenary review.

* * * * *

The First Circuit's decision creates a dangerous loophole in an important constitutional principle. If allowed to stand, that decision will "provide an easy mechanism for evasion" of sovereign immunity, because a plaintiff will readily be able to structure his claim to circumvent the traditional prohibition on retrospective relief. Pet. App. 63a (Lynch, C.J., dissenting from denial of rehearing en banc). The First Circuit's reasoning is plainly incorrect. And its holding is of obvious importance not only to the Commonwealth of Puerto Rico, but also to other sovereigns, as evidenced by the amicus participation of a majority of the States. For those reasons, we respectfully submit that the First Circuit's decision warrants further review and correction.

* * * * *

The petition for a writ of certiorari should be granted. The Court may wish to consider summarily reversing the judgment of the court of appeals; in the alternative, the Court should set the case for briefing and oral argument.

Respectfully submitted.

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No. 10-74

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*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## BRIEF FOR THE UNITED STATES AS AMICUS CURIAE


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## QUESTION PRESENTED

Whether the Eleventh Amendment prohibits a district court from entering an injunction requiring an official of the Commonwealth of Puerto Rico to adopt regulatory policies that will allow victims of prior unconstitutional actions by that official to recover previously lost funds from private consumers.

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*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

## BRIEF FOR THE UNITED STATES AS AMICUS CURIAE

This brief is submitted in response to the Court's order inviting the Acting Solicitor General to express the views of the United States. In the view of the United States, the petition for a writ of certiorari should be denied.

### STATEMENT

1. Respondents are the only two fresh milk processors in Puerto Rico. Pet. App. 3a. They are subject to extensive price regulations issued by a regulatory agency within the Puerto Rico Department of Agriculture that is known by its Spanish acronym, ORIL. As relevant here, ORIL has set a minimum price for respondents' purchase of raw milk from dairy farmers, as well as a maximum price for respondents' sale of processed milk to consumers. *Id.* at 5a; see, *e.g.*, 5 P.R. Laws Ann.

tit. 5, §§ 1093 (2005), 1096(a) (Supp. 2008), 1107(d) (Supp. 2008). In addition, respondents are required to purchase all of the dairy farmers' raw milk and to sell any surplus at a regulated price to an entity called Indulac. Pet. App. 6a & n.4. Beginning around 1985, Indulac started to produce UHT (non-refrigerated) milk, which competes directly with respondents' products. *Id.* at 6a, 8a. According to respondents' complaint in this case, although ORIL purportedly set respondents' rate of return at ten percent, respondents in fact lost millions of dollars in fiscal years 2001 through 2003. *Id.* at 9a-10a & n.10.

2. a. In 2004, respondents brought this action in the United States District Court for the District of Puerto Rico for declaratory and injunctive relief, alleging that ORIL's regulatory scheme violated the Just Compensation, Equal Protection, and Due Process Clauses of the Constitution. Pet. App. 11a. Petitioners moved to dismiss on numerous grounds. Among other things, they argued that it would violate the Eleventh Amendment for the district court to adjudicate respondents' claims that petitioners had violated Puerto Rico law. *Id.* at 205a, 207a. The district court agreed, and it dismissed those claims. *Id.* at 213a. Petitioners did not otherwise suggest that the relief respondents sought would violate the Eleventh Amendment, *id.* at 204a-207a, and in all other respects, the district court denied the motions to dismiss, *id.* at 218a.

The district court then held 51 evidentiary hearings regarding respondents' request for an injunction with respect to the regulatory scheme. Pet. App. 70a. The court ultimately issued a preliminary injunction requiring that (1) all processors (respondents and Indulac) pay the same price for raw milk; (2) the Administrator of

ORIL put into effect "rational and scientific regulatory standards that will allow him to determine costs and fair profits return for all the participants in the Puerto Rico regulated milk market"; and (3) the Administrator "adopt a temporary mechanism that will allow the processors to recover the new rate of return they are entitled to (whatever that may be) for the year 2003 (base cost year of the present structure) and up to the day when they begin to recover said rate based on the new regulatory standards and corresponding order." *Id.* at 196a-197a. With respect to the third requirement—the only part of the order that is at issue here—the district court stated that "[t]he Administrator may so act through regulatory accruals, special temporary rates of return or any other available mechanism of his choosing." *Id.* at 197a.

b. Petitioners attempted to comply with the district court's order through proposed regulations known as "Regulations No. 12." Defts.' Joint Informative Mot. Regarding Price Order and Regulation, Dist. Ct. Dkt. No. 938 (July 23, 2008) (Joint Informative Mot.); see Motion to Submit Certified Translation, Dist. Ct. Dkt. No. 1190 (Mar. 23, 2009). Regulations No. 12 provided for a special account, to be kept and managed by ORIL, that was to be used as a depository for the funds necessary to comply with the third part of the preliminary injunction and that would ultimately be disbursed to respondents. See Regulations No. 12, § 8. Those funds were to come from a surcharge of 1.5¢ per quart of milk sold by respondents. Pet. App. 22a n.17.

3. Petitioners appealed the preliminary injunction, and the court of appeals affirmed. Pet. App. 1a-44a. The court held that the third requirement in the district court's order did not violate the Eleventh Amendment.

*Id.* at 21a-28a. The court of appeals noted that, under *Ex parte Young*, 209 U.S. 123 (1908), the Eleventh Amendment does not bar suits against state officers in their official capacities to compel them to comply with federal law, although such suits may not seek retroactive monetary damages or equitable restitution from state resources. Pet. App. 23a. The court also noted that petitioners provided "no support for their contention that retrospective relief *that does not reach the state treasury* is barred by sovereign immunity." *Id.* at 25a. The court of appeals emphasized that, under the portion of the district court's order challenged here, "the money in question would come directly from consumers of milk in Puerto Rico," and the order "would, in no way, reach the coffers of the Commonwealth." *Id.* at 26a. Petitioners attempted to characterize the preliminary injunction as "ordering the payment of monetary damages in just compensation for a regulatory taking." *Ibid.* The court rejected that argument, observing that "here there has been no award of damages that the state must pay" because "[t]he district court's order does not require ORIL or the Department of Agriculture to provide just compensation, or any monetary award for that matter." *Id.* at 27a.

4. The court of appeals denied a petition for rehearing en banc. Pet. App. 46a.

a. Judge Torruella, concurring in the denial of rehearing en banc, noted that there was "no basis in the record" to conclude that the district court's order makes the Commonwealth liable for payment of monetary relief. Pet. App. 48a. He observed that the regulatory mechanism adopted to comply with the district court's order "carefully shields the Commonwealth's funds and resources from potential liability," rendering the "claim

that the Commonwealth would be required to pay a monetary judgment * * * speculative." *Id.* at 53a. Ultimately, Judge Torruella concluded that "[t]his case simply does not involve a monetary award against the state that burdens the state's treasury, nor does it implicate the Commonwealth's dignitary interests in a manner offensive to the Eleventh Amendment." *Id.* at 54a.

b. Judge Lynch dissented. Pet. App. 54a-68a. In her view, the injunction violated the Eleventh Amendment because it made "the Commonwealth, through one of its administrative agencies, liable for retrospective monetary relief." *Id.* at 60a.

## DISCUSSION

Petitioners argue that this Court's review is warranted because the district court issued an interlocutory order granting retrospective monetary relief against the Commonwealth of Puerto Rico. In fact, the district court's order merely requires changes to a program of administrative regulation that would allow respondents to increase the prices at which milk is sold to private parties in the future so that respondents can recover from past losses. That relief is consistent with the Eleventh Amendment, and the decision below does not conflict with any decision of this Court or of any court of appeals. The interlocutory posture of this case also weighs heavily against review. It is unclear whether funds would ultimately pass through a commonwealth account or not, and litigation regarding petitioners' attempts to comply with the preliminary injunction is continuing in the district court. The petition for a writ of certiorari should therefore be denied.

### A. The Judgment Of The Court Of Appeals Is Consistent With *Ex Parte Young*

1. The question presented in the petition (Pet. i) is whether a federal court may "order retrospective monetary relief against a sovereign." Petitioners assert that "the district court actually did impose[] monetary liability on the Commonwealth." Pet. Reply Br. 5. That assertion is erroneous, and petitioners' invocation of legal principles and case law applicable to "monetary" remedies is therefore misplaced. Pet. 4, 7, 9-17, 20-21; accord Pet. Reply Br. 1, 4-5.

Petitioners suggest that the court of appeals held that the preliminary injunction did not violate the Eleventh Amendment, "even assuming that the relief at issue was properly characterized as retrospective monetary relief." Pet. 16 (citing Pet. App. 25a-26a). That is incorrect. The court of appeals never assumed that the relief against petitioners could be characterized as monetary for purposes of Eleventh Amendment analysis. Instead, the court assumed that the relief could be characterized as *retrospective*, but it correctly held that the district court's order contains no relief against petitioners that is properly characterized as monetary. Pet. App. 25a-27a.

This suit was brought to challenge rates established under a regulatory program governing transactions between private parties. The district court's order directs the Administrator of ORIL to "adopt a temporary mechanism that will allow the processors to recover the new rate of return they are entitled to." Pet. App. 197a. Consistent with the nature of the regulatory program, the court's order does not mandate that the required recovery for respondents—or any part of it—come from the Commonwealth's funds, nor does it require petitioners

or the Commonwealth to use commonwealth funds if the "temporary mechanism" they choose is unsuccessful. To the contrary, the district court stated that the Administrator could comply with its order "through regulatory accruals, special temporary rates of return or *any other available mechanism of his choosing*," thus allowing the Commonwealth's own official to comply through an adjustment of rates charged by respondents to private parties and to ensure that no commonwealth funds are used. *Ibid.* (emphasis added).

It is uncontested that the Administrator has broad statutory authority to set the price of milk at all stages of its distribution. See 5 P.R. Laws Ann. tit. 5 § 1107(d) (Supp. 2008) ("The Administrator shall fix the maximum, minimum, or only prices for liquid milk * * * in all and any of the distribution channels and levels."). Using that authority, there are at least two obvious ways in which petitioners could have complied with the district court's order—that is, allowed the processors to recover an increased rate of return—without the use of commonwealth funds. First, petitioners could have raised the maximum price that processors were allowed to charge consumers for milk. Second, petitioners could have lowered the minimum price at which processors could purchase milk from dairy farmers. In other words, petitioners could have issued regulations that either allowed respondents to pay less for their raw milk or to charge more for their processed milk (or both). Either of those steps would have increased respondents' net income and thus allowed them to recover an increased rate of return in accord with the district court's order. And neither of these modes of complying with the district court's order would have involved the expenditure or obligation of commonwealth funds. Regardless of how petitioners

chose to comply with the district court's order, the fact that they had the ability to comply without spending or obligating commonwealth funds means that it is inaccurate to refer to the district court's order as "monetary relief." Cf. *Black's Law Dictionary* 920 (9th ed. 2009) (defining "money judgment" as "[a] judgment for damages subject to immediate execution, as distinguished from equitable or injunctive relief").*

Petitioners assert that "the district court has held the Commonwealth liable, and ordered it to set aside funds to cover that liability." Reply Br. 7; see State of Texas, et al., Amicus Br. 18 (suggesting that the court "order[ed] a future payment from a designated account created by the State's regulatory powers"); Pet. App. 64a (Lynch, J., dissenting) (arguing that "[t]he injunction orders the Administrator of ORIL to use the state's regulatory, revenue-raising powers to satisfy plaintiffs' demand for compensation"). But the district court's order reveals that it did not require such an arrangement. *Id.* at 196a-198a. As noted above, the district court did not order that *any* funds be "set aside." Petitioners can comply with the order without any such set aside and independent of any commonwealth funds.

At bottom, there is no meaningful difference between the relief ordered by the district court in this case and that at issue in *Ex parte Young*, 209 U.S. 123 (1908). Like this case, *Ex parte Young* involved state officials

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* Raising the price that processors could charge to consumers could affect the public fisc of Puerto Rico to the extent that the Commonwealth is a purchaser of milk. Petitioner has not suggested that such an indirect financial effect in the marketplace would be relevant for Eleventh Amendment purposes. In any event, decreasing the price that producers could charge the processors would not have even that attenuated potential effect on the Commonwealth as consumer.

who had regulated an industry by setting rates so low as to be unconstitutionally confiscatory. *Id.* at 148-149. This Court concluded that the Eleventh Amendment did not bar a federal court from enjoining the State officials' attempts to enforce the unconstitutionally low rate. See *id.* at 149. Although the ruling resulted in an increase in the flow of money from customers to members of the regulated industry, that did not convert the relief obtained from equitable relief to monetary relief against the commonwealth officials, nor did it mean that the relief violated the Eleventh Amendment. Petitioners identify no basis on which to depart from the result in *Ex parte Young*.

2. Petitioners chose to employ a particular money-handling mechanism that was not mandated by the district court—a surcharge collectible by the Commonwealth and then paid to the processors, rather than an increase in the maximum price that the processors are allowed to charge their customers directly or a decrease in the maximum price that dairy farmers are allowed to charge the processors directly. That choice by petitioners does not alter the sovereign-immunity analysis. This case came to the court of appeals as an appeal from the district court's preliminary injunction. What is at issue is what the district court's order requires, not what steps petitioners have chosen to take in response to that order. The district court could simply have ordered petitioners to increase the maximum allowable price for milk sold by processors (or to decrease the maximum allowable price for milk sold to processors) by an amount that would allow the processors to recover the appropriate rate of return. Instead, respecting Puerto Rico's dignitary interests, the court permitted petitioners to choose whatever method of compliance they

deemed appropriate, so long as it produced the legally required result. See *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602-603 (1944). As noted above, the court's order does not require the use or obligation of commonwealth funds. Having been accorded discretion to determine how to ensure that respondents obtained the necessary return, petitioners cannot complain that the specific way in which they have exercised that discretion contemplates the payment of a surcharge into a special account under the auspices of ORIL.

Nor is there merit to petitioners' suggestion that the Eleventh Amendment was violated simply because the complaint sought monetary relief. See, *e.g.*, Pet. Reply Br. 5 (asserting that "[s]imply by virtue of the fact that respondents were *seeking* a court order awarding monetary relief against the Commonwealth for past constitutional violations, this case implicates the Commonwealth's sovereign immunity"); *id.* at 3-4, 7. The proper time to challenge the relief sought in a complaint is in a motion to dismiss. Here, although petitioners filed motions to dismiss, they did not allege that the relief sought would violate the Eleventh Amendment to the extent it was based on violations of the United States Constitution. Nor did they appeal the denial of their motions to dismiss. Whether or not those failures amounted to a waiver, petitioners did not squarely challenge the propriety of the relief sought for the alleged constitutional violation, and this Court's review of that issue would therefore be unwarranted. That is particularly so now that the litigation has progressed to the point at which the district court has granted preliminary injunctive relief, and only the propriety of the relief actually granted is directly at issue.

3. Petitioners suggest (Pet. 8-9) that even non-monetary relief is barred by sovereign immunity if it is "retrospective" in nature, but that is incorrect. Petitioners rely on *Green* v. *Mansour*, 474 U.S. 64 (1985), in which this Court held that a district court lacked authority to issue a declaratory judgment that state officials had violated federal law in the past. Petitioners' reliance on that case is misplaced. In *Green*, the Court emphasized both the absence of any "claimed continuing violation of federal law" and the fact that "the issuance of a declaratory judgment" in the circumstances of that case "would have [had] much the same effect as a full-fledged award of damages or restitution by the federal court" because "it might be offered in state-court proceedings as res judicata on the issue of liability, leaving to the state courts only a form of accounting proceeding whereby damages or restitution would be computed." *Id.* at 73. Neither of those considerations is present here. First, respondents alleged—and the district court found—an ongoing constitutional violation. Pet. App. 171a. Second, as explained above, the order at issue here does not require any payment of money to or by Puerto Rico or its officials. And as this Court has more recently explained, so long as "no past liability of the State, or of any of its [officials], is at issue," and the court's order "does not impose *upon the State* 'a monetary loss resulting from a past breach of a legal duty on the part of the defendant state officials,'" a court may permissibly declare "the *past*, as well as the *future*," illegality of official action, "so that the past financial liability of private parties may be affected." *Verizon Md. Inc.* v. *Maryland Pub. Serv. Comm'n*, 535 U.S. 635, 646 (2002) (quoting *Edelman* v. *Jordan*, 415 U.S. 651, 668 (1974)).

In any event, it is far from clear that the relief at issue in this case is appropriately characterized as retrospective. In setting the prices at which respondents may purchase and sell milk, petitioners enjoy considerable discretion, but they are constitutionally required to permit respondents to earn a just and reasonable rate of return on their invested capital if that is the basis for the fixing of rates under the regulatory program. *Duquesne Light Co.* v. *Barasch*, 488 U.S. 299, 307-316 (1989); *Hope Natural Gas Co.*, *supra*. Here, the district court found that the years of losses suffered by respondents as a result of petitioners' regulatory scheme had eroded their capital base, making it necessary to take account of those losses in order to determine how milk prices should be regulated in the future. Pet. App. 118a. In other words, at least some consideration of past actions was appropriate in order to provide effective relief from ongoing violations and to set future regulation on a proper course. Such relief is appropriately characterized as prospective, and it is consistent with the Eleventh Amendment. See *Milliken* v. *Bradley*, 433 U.S. 267, 290 (1977).

**B. The Judgment Below Does Not Conflict With Any Decision Of Any Other Court Of Appeals**

According to petitioners (Pet. 10-13), the decision below is contrary to the decisions of five other courts of appeals. But because the district court did not order monetary relief against petitioners or the Commonwealth—and because petitioners can comply with the district court's order without using any funds that were ever under the control of the Commonwealth—petitioners' assertion is incorrect. Each of the decisions cited by petitioners involved actions seeking pay-

ment from a State's funds. Three of those decisions involved state funds in specific segregated accounts, see Pet. 10-13 (citing *Ernst* v. *Rising*, 427 F.3d 351, 361-362 (6th Cir. 2005) (en banc), cert. denied, 547 U.S. 1021 (2006); *Paschal* v. *Jackson*, 936 F.2d 940, 944 (7th Cir. 1991), cert. denied, 502 U.S. 1081 (1992); *Esparza* v. *Valdez*, 862 F.2d 788, 794 (10th Cir. 1988), cert. denied, 492 U.S. 905 (1989)), and the other two involved state funds that would, if lost, be reimbursed by the federal government, see Pet. 11-12 (citing *Florida Ass'n of Rehab. Facilities, Inc.* v. *Florida Dep't of Health & Rehabilitative Servs.*, 225 F.3d 1208, 1225 (11th Cir. 2000); *Cronen* v. *Texas Dep't of Human Servs.*, 977 F.2d 934, 938 (5th Cir. 1992)). Here, by contrast, petitioners can comply with the district court's order without using any commonwealth funds.

For the same reason, this case does not implicate the question, posed by petitioners, "whether there are some state funds that do not enjoy Eleventh Amendment immunity," Pet. 14 (quoting *Brown* v. *Porcher*, 459 U.S. 1150, 1153 (1983) (White, J., dissenting from the denial of certiorari)), and that question is therefore irrelevant. Likewise, the petition's entire discussion of the importance of the issue presented (Pet. 19-21) is misplaced because it rests on the erroneous premise that the decision below allows the award of retrospective monetary relief against States. The reality that the district court did not order monetary relief here thus weighs heavily against granting the petition.

### C. This Case Would In Any Event Be An Inappropriate Vehicle For Considering The Question Presented

1. Even if the question presented, as formulated by petitioners, were actually presented and otherwise mer-

ited this Court's consideration, review would be unwarranted at this time because the case is still in an interlocutory posture. The Court routinely denies certiorari petitions filed by parties challenging interlocutory determinations that may be reviewed at the conclusion of the proceedings. See, *e.g.*, *VMI* v. *United States*, 508 U.S. 946 (1993) (Scalia, J., respecting denial of certiorari); *Hamilton Brown Shoe Co.* v. *Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916) (describing the interlocutory nature of a decision as "a fact that of itself alone furnishe[s] sufficient ground for the denial of" certiorari). That practice ensures that all of a party's claims will be consolidated and presented in a single petition. Here, the interests of judicial economy would be best served by denying review now and allowing petitioners to reassert all of their claims upon the entry of a final judgment, if they still wish to do so at that time.

Petitioners acknowledge (Pet. Reply Br. 6) that the preliminary injunction at issue in this case is interlocutory, but they suggest that the general rule against interlocutory review does not apply in cases involving sovereign immunity because the benefit of such immunity is lost if the existence of the immunity is not finally determined until after trial. That logic does not apply here because petitioners do not seek review of the denial of a motion to dismiss on sovereign-immunity grounds, nor do they contend that this Court should remand with instructions to dismiss. Instead, the only issue presented by the petition is the propriety of the preliminary injunction issued by the district court. Thus, even if this Court were to grant review and reverse the judgment of the court of appeals, litigation against petitioners would continue. This Court's intervention would therefore not protect Puerto Rico from continued litigation or trial.

2. Review at this stage would be inappropriate for the additional reason that it remains unclear how petitioners will comply with the district court's preliminary injunction. Changes in their method of compliance could alter the appropriate analysis of the Eleventh Amendment issues raised by the petition.

In arguing that review is appropriate now, petitioners refer to "a regulation and accompanying administrative order imposing a 1.5¢ surcharge on every quart of milk sold in Puerto Rico," and they further state that "proceeds from the surcharge *were to have been* held in a segregated account by the Milk Industry Development Fund." Pet. 4 (emphasis added). Petitioners rely heavily on the fact that the funds are required to flow through that segregated account, but the status of that requirement is uncertain. While petitioners cite no specific regulatory provisions, it appears that the regulations to which they refer are Regulations No. 12, which they submitted to the district court in 2008. But when petitioners submitted those regulations to the court, they made clear that they were not final. See Joint Informative Mot. 1-2 (referring to Regulations No. 12 as a "draft" and a "proposed regulation"); see also Vaquería Tres Monjitas Br. in Opp. 10 (suggesting that there is no legal requirement that funds from the surcharge be given to the Commonwealth, only a "proposed * * * regulation" that "has not yet taken effect"). Moreover, we are informed by the parties that the 1.5¢ surcharge contemplated by Regulations No. 12 is currently being collected and maintained in a separate account by respondents, not by any government agency or official.

The status of Regulations No. 12 has been litigated since the preliminary injunction was initially issued, and the parties have disputed whether Regulations No. 12

and related ORIL orders comply with the preliminary injunction. See, *e.g.*, Dist. Ct. Dkt. Nos. 938, 966, 968-970, 973, 978, 981, 982, 985 (party filings addressing Regulations No. 12). The district court has ordered petitioners to modify Regulations No. 12 in various respects, Amended Opinion and Order, Dist. Ct. Dkt. No. 1697 (Sept. 22, 2010), and it has emphasized that "ORIL, at this time, is not near a final decision as to the remedy relating to * * * a fair return of equity." Opinion and Order 4, Dist. Ct. Dkt. No. 1804 (Jan. 3, 2011). In February, petitioners filed a notice of interlocutory appeal from the district court's recent orders. Defts.' Notice of Appeal, Dist. Ct. Dkt. No. 1868 (Feb. 2, 2011). This Court should not review the preliminary injunction while its implementation continues to be the source of dispute and uncertainty being litigated below, and while no funds from the surcharge are actually being paid to a special account maintained by ORIL.

3. Finally, this case is an inappropriate vehicle for considering the sovereign-immunity issues raised in the petition because it arises in the unusual context of Puerto Rico. This Court has expressly reserved judgment on whether Puerto Rico should be treated as a State for Eleventh Amendment purposes. *Puerto Rico Aqueduct & Sewer Auth.* v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 n.1 (1993). Petitioners suggest (Pet. Reply Br. 7) that the Court could "decide this case on the assumption that Puerto Rico is entitled to sovereign immunity," but that is incorrect. Unlike *Puerto Rico Aqueduct & Sewer Authority*, which involved the appealability of a sovereign-immunity claim, this case presents a substantive question of the scope of immunity, and the Court could not reverse the judgment of the court of

appeals without holding, at least implicitly, that Puerto Rico enjoys such immunity.

Whatever inherent immunity a territory such as Puerto Rico might enjoy, it does not necessarily have the same scope as that of States, which entered the Union under a constitutional compact that has been understood to confirm their immunity from suit. Cf. *Blatchford* v. *Native Village of Noatak*, 501 U.S. 775, 780-782 (1991). Because the applicability of the Eleventh Amendment to Puerto Rico is unsettled and could provide an alternative basis for affirming the judgment below, this case is a particularly poor vehicle for resolving the question presented in the certiorari petition.

## CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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No. 10-74

# In the Supreme Court of the United States

JAVIER RIVERA AQUINO, SECRETARY, PUERTO RICO DEPARTMENT OF AGRICULTURE, ET AL., PETITIONERS

*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

**BRIEF FOR TEXAS, ARKANSAS, COLORADO, DELAWARE, FLORIDA, GEORGIA, HAWAII, IDAHO, ILLINOIS, INDIANA, LOUISIANA, MAINE, MARYLAND, MASSACHUSETTS, MICHIGAN, MISSISSIPPI, MONTANA, NEVADA, OHIO, OKLAHOMA, PENNSYLVANIA, SOUTH CAROLINA, TENNESSEE, UTAH, VERMONT, AND VIRGINIA AS AMICI CURIAE SUPPORTING PETITIONERS**

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# In the Supreme Court of the United States

No. 10-74

JAVIER RIVERA AQUINO, SECRETARY, PUERTO RICO DEPARTMENT OF AGRICULTURE, ET AL., PETITIONERS

*v.*

SUIZA DAIRY, INC., ET AL.

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIRST CIRCUIT*

**BRIEF FOR TEXAS, ARKANSAS, COLORADO, DELAWARE, FLORIDA, GEORGIA, HAWAII, IDAHO, ILLINOIS, INDIANA, LOUISIANA, MAINE, MARYLAND, MASSACHUSETTS, MICHIGAN, MISSISSIPPI, MONTANA, NEVADA, OHIO, OKLAHOMA, PENNSYLVANIA, SOUTH CAROLINA, TENNESSEE, UTAH, VERMONT, AND VIRGINIA AS AMICI CURIAE SUPPORTING PETITIONERS**

## INTEREST OF AMICI CURIAE[1]

Petitioners are correct that the First Circuit's decision significantly—and erroneously—expands the doctrine of *Ex parte Young* and thereby portends "profound consequences for other sovereigns." Pet. 21. According to the holding below, settled principles of sovereign immunity vanish whenever an award of

[1] Pursuant to this Court's Rule 37.2(a), counsel of record for all parties received timely notice of amici curiae's intent to file this brief, and consented to it.

retrospective monetary relief is not satisfied directly from the public fisc. This is true, according to that decision, even where state officials (in their official capacity) are *judicially compelled* to invoke the State's core regulatory powers to fund the compensatory award. This case thus presents exceptionally important questions concerning sovereign immunity, the *Ex parte Young* doctrine, and the susceptibility of state officials to claims for retrospective relief. In light of its plain "importance" and its high "stakes for the [S]tates in the many cases in which individuals seek compensation for past constitutional violations," Pet. App. 56a (Lynch, J., dissenting from denial of rehearing en banc), the amici States have a distinct interest in the correct disposition of this matter.

## DISCUSSION

The First Circuit held that sovereign immunity does not bar the imposition of retrospective relief against a State (through its officials) unless public funds are directly extracted from the state treasury. Pet. App. 21a-28a. This decision conflicts with the uniform view of every other circuit to have considered this question under the prevailing framework—and it does so by sharply departing from this Court's settled jurisprudence in the area.

Under established law, respondents cannot pierce the Commonwealth's sovereign immunity—which otherwise categorically bars any official-capacity suit—without invoking the narrow exception found in *Ex parte Young*. That exception is limited to vindicating the federal interest in securing *prospective* compliance with federal law—and it emphatically does not authorize courts to order

retrospective relief. There accordingly is no basis in law or logic for suggesting (as the First Circuit incorrectly did) that immunity principles turn on the *source* of any compensatory funds rather than the character (prospective or otherwise) of the State's putative violation. Because both the strict letter and underlying rationale of *Ex parte Young* are carefully calibrated to avoid retrospective impositions on sovereign entities, the First Circuit was incorrect to upset this delicate balance.

Moreover, the decision below is wrong even on its own terms. There is no difference, practically or legally, between (i) an order compelling a State to collect and deposit funds into a specific account earmarked for retrospective monetary relief (which the court below deemed permissible) and (ii) an order compelling a State to collect funds deposited *into the general treasury* and earmarked for the same retrospective relief (which even the court below found impermissible). The source of the funds is still the same citizenry compelled to contribute public money to the same cause based on the same exercise of regulatory power. There is no magic (much less constitutional significance) to the location where the funds are stored—and no less interference with the State's sovereign authority to determine when and how to collect and disburse public funds.

Nor is that interference at all insubstantial. The district court's order, upheld by the First Circuit, authorized the federal judiciary to commandeer state officials and compel them to invoke the Commonwealth's regulatory machinery. The court of appeals was surely correct that this directive served to avoid a plainly impermissible judicial decree for a

retrospective lump-sum payment. But the court was just as surely mistaken that this sort of end-run is consistent with the States' role as co-equal sovereigns in our federalist system, or permissible in any way under established principles of sovereign immunity.

Because this decision is "flatly contrary to this Court's controlling precedent," *Arkansas* v. *Sullivan*, 532 U.S. 769, 771 (2001) (per curiam), the States respectfully submit that summary reversal is appropriate under these circumstances. See Sup. Ct. R. 16.1; Eugene Gressman et al., *Supreme Court Practice* § 5.12(a), (c) (9th ed. 2007). This Court has invoked that procedure in the past to protect state sovereign immunity, see, *e.g.*, *Fla. Dep't of Health & Rehabilitative Servs.* v. *Fla. Nursing Home Ass'n*, 450 U.S. 147 (1981) (per curiam); *Alabama* v. *Pugh*, 438 U.S. 781 (1978) (per curiam), and it should do so here. At a minimum, the petition should be granted.

**A. Absent An Unmistakable Waiver Or Explicit Abrogation, Sovereign Immunity Bars Federal Courts From Imposing Retrospective Relief In Private Suits Against States Or State Officials In Their Official Capacities**

1. The law governing the correct disposition of this case is so settled that it barely requires any discussion at all. Sovereign immunity prevents a private party from subjecting a State to suit without its consent. See, *e.g.*, *Alden* v. *Maine*, 527 U.S. 706, 712-713 (1999); *Idaho* v. *Coeur d'Alene Tribe*, 521 U.S. 261, 267-268 (1997); *Ex parte New York*, 256 U.S. 490, 497 (1921); *Hans* v. *Louisiana*, 134 U.S. 1, 9-21 (1890). The doctrine protects a State's dignity

and its treasury, *e.g.*, *Seminole Tribe* v. *Florida*, 517 U.S. 44, 58 (1996); these fundamental interests were of such central concern to the Founders that the judiciary's initial failure to recognize the States' immunity was met with an immediate constitutional amendment, see *Coll. Sav. Bank* v. *Fla. Prepaid Postsecondary Educ. Expense Bd.*, 527 U.S. 666, 669 (1999) (describing the Eleventh Amendment's swift passage in response to *Chisholm* v. *Georgia*, 2 U.S. (2 Dall.) 419 (1793)); see also *Alden*, 527 U.S. at 720. Nor may parties evade the immunity bar (or undercut its underlying interests) by suing a State's agencies or its officials: a suit against a state official, in his or her official capacity, is deemed equivalent to a suit against the State itself, and so the full immunity protecting the sovereign applies. See, *e.g.*, *Pennhurst State Sch. & Hosp.* v. *Halderman*, 465 U.S. 89, 100-102 (1984); *Ford Motor Co.* v. *Dep't of Treasury*, 323 U.S. 459, 462-464 (1945); *Poindexter* v. *Greenhow*, 114 U.S. 270, 287 (1885).[2]

2. The Court in *Ex parte Young*, 209 U.S. 123 (1908), created an important exception to this Eleventh Amendment immunity- but one narrow in

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[2] This brief refers to *States* and *state sovereign immunity* because the First Circuit has long held that the Commonwealth of Puerto Rico and amici States are identical for purposes of sovereign-immunity analysis. See, *e.g.*, *Diaz-Fonseca* v. *Puerto Rico*, 451 F.3d 13, 33 (1st Cir. 2006), Pet. 7 n.1. This brief also employs the phrase *Eleventh Amendment immunity* as a "convenient shorthand," *Alden*, 527 U.S. at 713. "[T]he Eleventh Amendment does not define the scope of the States' sovereign immunity; it is but one particular exemplification of that immunity." *Fed. Mar. Comm'n* v. *S.C. State Ports Auth.*, 535 U.S. 743, 753 (2002).

scope and carefully tethered to its animating rationale. See, *e.g.*, *P.R. Aqueduct & Sewer Auth.* v. *Metcalf & Eddy, Inc.*, 506 U.S. 139, 146 (1993) (noting the "exception").

In *Ex parte Young*, the Court allowed a private party to pursue prospective injunctive relief in federal court against a state official to enjoin the enforcement of an unconstitutional state statute. In doing so, the Court avoided the issue of sovereign immunity by treating the suit as if it ran only against the official himself, rather than the State—in a manner the Court has characterized as a "fiction," given the traditional view that sovereign immunity extends to suits against state officials (in their official capacity) as well as States. See, *e.g.*, *Cent. Va. Cmty. Coll.* v. *Katz*, 546 U.S. 356, 378 n.14 (2006) (referring to *Ex parte Young* doctrine "as an expedient 'fiction' necessary to ensure the supremacy of federal law"); *Coeur d'Alene*, 521 U.S. at 270 (referring to "the *Young* exception" as "an obvious fiction"). The Court reasoned that officials cannot invoke the State's immunity when they violate federal law because all unconstitutional statutes are void: without the protection of the (void) state statute, an official is "stripped of his official or representative character and * * * subjected in his person to the consequences of his individual conduct." *Ex parte Young*, 209 U.S. at 159-160.

This exception, however, is not categorical in nature, and it hardly "insulate[s] from Eleventh Amendment challenge every suit in which a state official is the named defendant." *Papasan* v. *Allain*, 478 U.S. 265, 277 (1986). See also *Pennhurst*, 465 U.S. at 102 ("[T]he theory of *Young* has not been

provided an expansive interpretation."); Richard H. Fallon, Jr. et al., *Hart and Wechsler's The Federal Courts and The Federal System* 892-896 (6th ed. 2009). On the contrary, the Court constrained the *Ex parte Young* doctrine in *Edelman* v. *Jordan*, 415 U.S. 651 (1974), recognizing a "distinction between prospective and retroactive relief [that] continues to lie at the center of the Court's Eleventh Amendment jurisprudence," 1 Laurence H. Tribe, *American Constitutional Law* 559 (3d ed. 2000). "The distinction between that relief permissible under the doctrine of *Ex parte Young* and that found barred in *Edelman* was the difference between prospective relief on one hand and retrospective relief on the other." *Quern* v. *Jordan*, 440 U.S. 332, 337 (1979).

These limits on *Ex parte Young* reflect the doctrine's underlying rationale. In restricting relief to prospective remedies, the Court struck an important balance between the need to protect the primacy of federal law (as required by the Supremacy Clause) and the countervailing need to protect sovereign immunity (as required by the underlying constitutional structure). See *Pennhurst*, 465 U.S. at 106 (describing the limits as "reconcil[ing] competing interests" in "vindicat[ing] the supreme authority of federal law" and "preserving to an important degree the constitutional immunity of the States"). Well aware of "the role of the [Eleventh] Amendment in our system of federalism," *P.R. Aqueduct*, 506 U.S. at 146, the Court has carefully avoided "stretch[ing] [*Ex parte Young*] too far and * * * upset[ting] the balance of federal and state interests that it embodies," *Papasan*, 478 U.S. at 277. A sensitive calibration of

the "proper scope and application" of *Ex parte Young* therefore "ensure[s] that the doctrine of sovereign immunity remains meaningful, while also giving recognition to the need to prevent violations of federal law." *Coeur d'Alene*, 521 U.S. at 269.

These general principles lead to a settled standard for evaluating a suit in federal court against a sovereign State and its officials. "In determining whether the doctrine of *Ex parte Young* avoids an Eleventh Amendment bar to suit, a court need only conduct a 'straightforward inquiry into whether [the] complaint alleges an ongoing violation of federal law and seeks relief properly characterized as prospective.'" *Verizon Md. Inc.* v. *Pub. Serv. Comm'n*, 535 U.S. 635, 645 (2002) (alteration in original) (quoting *Coeur d'Alene*, 521 U.S. at 296 (O'Connor, J., concurring in part and concurring in the judgment)). In focusing on ongoing violations and prospective relief, *Ex parte Young* secures compliance with federal law without unduly intruding into the sphere of state autonomy.

### B. Contrary To The Decision Below, Sovereign Immunity Precludes Any Retrospective Monetary Relief Against A State Entity—No Matter The Source Of The Funds

In its decision below, the First Circuit held that sovereign immunity is inapplicable in official-capacity suits so long as no money is ultimately extracted from the state treasury. Specifically, under the panel's view, any State can be forced by judicial decree to collect funds from its citizens and deliver them to private plaintiffs as compensation for past harms. That view is fundamentally mistaken.

Indeed, the judgment below conflicts with the "straightforward inquiry" reaffirmed in *Verizon*, 535 U.S. at 645, and reflected in the consistent teachings of this Court's precedent since *Ex parte Young*. It upends the entrenched distinction between prospective and retrospective relief and replaces it with an unprecedented focus on state treasuries. It also wrongly concludes that an order commandeering state officials to regulate in their official capacity has no implications at all for the State's sovereignty. Contrary to the panel's opinion, this new approach is impossible to square with the existing jurisprudential framework. It should be rejected.

1. The court of appeals failed to adhere to either the explicit dictates or the underlying rationale of *Ex parte Young*. To be sure, the decision below does reference *Edelman*'s distinction between prospective and retrospective relief in the *Ex parte Young* context. Pet. App. 23a. According to the panel, however, "the Eleventh Amendment's prohibition against retrospective relief does not apply" unless "state funds are implicated." *Id.* at 26a. This novel idea drives the decision below. See, *e.g.*, *id.* at 24a (agreeing that "even if the form of relief is deemed retroactive, sovereign immunity should present no bar, as none of the compensation would come from the state treasury"); *id.* at 25a (rejecting the "contention that retrospective relief *that does not reach the state treasury* is barred by sovereign immunity"); *id.* at 47a (Torruella, J., concurring in denial of rehearing en banc) (asserting that the panel correctly "place[d] decisive weight on the impact a judgment has on the state treasury").

This view is irreconcilable with controlling precedent. As *Edelman* established, the fiction of *Ex parte Young* applies only to claims for prospective relief—a necessary condition that must be satisfied at the outset. See *Coeur d'Alene*, 521 U.S. at 270 (majority opinion) (noting *Edelman*'s "limitation * * * of *Young* to prospective relief"); *Milliken* v. *Bradley*, 433 U.S. 267, 289 (1977) (noting "the prospective-compliance exception reaffirmed by *Edelman* * * * which had its genesis in *Ex parte Young*"); *Edelman*, 415 U.S. at 664, 665, 666 n.11, 677 (noting that *Ex parte Young* awarded only prospective relief). This Court has repeatedly distinguished between prospective and retrospective relief, and with good reason. The point of *Ex parte Young*'s balancing is to vindicate the federal interest in securing compliance with federal law without unduly infringing upon the State's constitutional interest in its underlying sovereignty. A federal court can halt an ongoing violation by ordering prospective injunctive relief, thereby ensuring the supremacy of federal law. Retrospective relief, by contrast, cannot prevent past violations of federal law involving conduct already completed. This is why the Court's precedent "does not bar only retroactive monetary relief, but rather *all* retroactive relief." *S & M Brands, Inc.* v. *Cooper*, 527 F.3d 500, 509 (6th Cir. 2008).

The decision in *Green* v. *Mansour*, 474 U.S. 64 (1985), is illustrative. In *Green*, private plaintiffs sued state officials for calculating welfare benefits in violation of federal law. *Id.* at 65. Congress changed the law while the suit was pending, bringing the officials' conduct into compliance and mooting any claim for prospective relief. *Ibid.* Plaintiffs

nevertheless sought "notice relief"—a non-monetary form of relief simply providing information to plaintiffs' class about putatively wrongful past conduct—along with a declaratory judgment that prior calculations had violated federal law. *Ibid.*

The Court articulated its rationale at the outset:

> Both prospective and retrospective relief implicate Eleventh Amendment concerns, but the availability of prospective relief of the sort awarded in *Ex parte Young* gives life to the Supremacy Clause. Remedies designed to end a continuing violation of federal law are necessary to vindicate the federal interest in assuring the supremacy of federal law. But compensatory or deterrence interests are insufficient to overcome the dictates of the Eleventh Amendment.

474 U.S. at 68 (citations omitted).

Although the notice relief called for no payments from the state treasury, the Court declared it barred by state sovereign immunity because it was purely retrospective and in no way ancillary to any prospective relief: "Because 'notice relief' is not the type of remedy designed to prevent ongoing violations of federal law, the Eleventh Amendment limitation on the Art. III power of federal courts prevents them from ordering it as an independent form of relief." 474 U.S. at 71. The Court likewise held that state sovereign immunity prevented issuance of a backwards-looking declaratory judgment because such relief would open the state officials to monetary liability in state court and thus enable "a partial 'end run' around [*Edelman*]." *Id.* at

73. *Green* thus reaffirmed the distinction between prospective and retrospective relief, while demonstrating, through its denial of notice relief, that an impact on the state treasury is not a necessary condition for a sovereign immunity bar.

The decision below stands in stark contrast to this controlling analysis. The relief upheld by the First Circuit against a sovereign immunity challenge—a judicially imposed surcharge of 1.5¢ for every quart of milk sold in Puerto Rico, Pet. App. 22a & n.17—is even more detrimental to the precepts of sovereign immunity than the notice relief condemned in *Green*. The milk surcharge is retrospective. See *Buckhanon* v. *Percy*, 708 F.2d 1209, 1215 (7th Cir. 1983) ("[T]he date for determining whether a monetary award is retroactive or prospective is that upon which the district court determined that the state's conduct was wrongful." (citing *Fitzpatrick* v. *Bitzer*, 427 U.S. 445, 451 (1976))). The district court granted the preliminary injunction on July 13, 2007, Pet. App. 69a, at which time it ordered petitioners "to adopt a temporary mechanism that will allow [respondents] to recover the new rate of return * * * for the year 2003 * * * and up to the day when they begin to recover said rate based on the new regulatory standards and corresponding order," *id.* at 197a. The panel defended this relief on the ground that the milk surcharge requires no payments from the state treasury. Pet. App. 26a (finding that "no state funds are implicated"); contra *id.* at 65a-66a (Lynch, J., dissenting from denial of rehearing en banc) (arguing that "[t]his is plainly relief that reaches the state fisc"). But here, as in *Green*, the retrospective milk surcharge should be barred by

Eleventh Amendment immunity irrespective of its effect, if any, on the state treasury—the threshold for setting aside sovereign immunity (read: *prospective* relief) was not met.

It has been said that "the difference between the type of relief barred by the Eleventh Amendment and that permitted under *Ex parte Young* will not in many instances be that between day and night." *Edelman*, 415 U.S. at 667. This difficulty is present in cases where the line separating prospective from retrospective relief is elusive. See, *e.g.*, *Missouri* v. *Jenkins*, 515 U.S. 70, 132 n.5 (1995) (Thomas, J., concurring) (noting the conceptual difficulty). But this is no such case. This case involves an obvious example of retrospective relief; the panel below simply refused to recognize that the prospective nature of any relief is a necessary (not merely sufficient) condition for invoking any exception to the States' sovereign immunity. This Court has cautioned that "extend[ing] the fiction of [*Ex parte*] *Young* to encompass retroactive relief * * * would effectively eliminate the constitutional immunity of the States." *Pennhurst*, 465 U.S. at 105. Yet the decision below, if allowed to stand, would endorse just such an expansion—and compel a corresponding detraction from the core principles underpinning sovereign immunity. For that reason alone, the decision should be swiftly reversed.

2. Nor is the First Circuit correct that sovereign immunity is not implicated in the first place (rendering the prospective/retrospective distinction irrelevant) unless funds from the state treasury are immediately at risk. This contention is twice wrong. As an initial matter, the principle of sovereign

immunity is not so limited in scope—indeed, controlling precedent establishes that exactly the opposite is true. And in any event, when public funds are levied, collected, and remitted by direct compulsion of state law, there is no material distinction between fees deposited in a separate account and fees deposited in the state treasury.

a. The First Circuit's mistaken conclusion follows directly from its flawed premise that sovereign immunity protects a State's treasury and virtually nothing else. This view "reflects a fundamental misunderstanding of the purposes of sovereign immunity." *S.C. State Ports Auth.*, 535 U.S. at 765. Absent from the First Circuit's account is an acknowledgement of the States' central interest in their independence as one half of our system of dual sovereignty—and the States' related (and well recognized) dignity inherent in "their status as residuary sovereigns and joint participants in the governance of the Nation." *Alden*, 527 U.S. at 748.

In isolating its focus on the state treasury, the court of appeals is correct, of course, that a private party cannot sue a state official for compensatory damages drawn from the public fisc. *E.g.*, *Edelman*, 415 U.S. at 663 (citing *Ford Motor Co.*, 323 U.S. at 464). But sovereign immunity does not start and stop with the public fisc; it extends further and protects against all other forms of retrospective relief. See *Frew ex rel. Frew* v. *Hawkins*, 540 U.S. 431, 437 (2004) ("Federal courts may not award retrospective relief, *for instance*, money damages or its equivalent, if the State invokes its immunity." (emphasis added)); *Coeur d'Alene*, 521 U.S. at 288 (O'Connor, J., concurring in part and concurring in

the judgment) ("A federal court cannot award retrospective relief, designed to remedy past violations of federal law." (citation omitted)); *id.* at 298-299 (Souter, J., dissenting) ("The plaintiff * * * must seek prospective relief to address an ongoing violation, not compensation *or other retrospective relief* for violations past." (emphasis added)); cf. *Cory* v. *White*, 457 U.S. 85, 90 n.2 (1982) ("*Edelman* recognized the rule that a suit by private parties seeking to impose a liability which must be paid from public funds in the state treasury is barred by the Eleventh Amendment, but *never asserted that such suits were the only ones so barred.*" (citation and internal quotation marks omitted; emphasis added)).

The court of appeals is consequently incorrect that this Court has "consistently considered the source of relief as being of paramount importance to Eleventh Amendment considerations." Pet. App. 25a (citing *Hess* v. *Port Auth. Trans-Hudson Corp.*, 513 U.S. 30 (1994)). Instead, "[t]he preeminent purpose of state sovereign immunity is to accord States the *dignity* that is consistent with their status as sovereign entities." *S.C. State Ports Auth.*, 535 U.S. at 760 (emphasis added). Although protecting the state treasury is a weighty concern, safeguarding the dignity of the States has also assumed a crucial role in this Court's sovereign-immunity jurisprudence. See, *e.g.*, *Coeur d'Alene*, 521 U.S. at 268 (noting "the dignity and respect afforded a State, which the immunity is designed to protect"); *Seminole Tribe*, 517 U.S. at 58 ("The Eleventh Amendment does not exist solely in order to 'preven[t] federal-court judgments that must be paid out of a State's treasury,' [*Hess*, 513 U.S. at 48]; it also serves to

avoid 'the indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties,' [*P.R. Aqueduct*, 506 U.S. at 146]."). Nor is this dignity rationale a theoretical novelty. See *In re Ayers*, 123 U.S. 443, 505 (1887) ("The very object and purpose of the 11th Amendment were to prevent the indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties."). Indeed, the dignity rationale is so commonplace that it even appears in the single Supreme Court opinion referenced by the First Circuit in support of its unduly narrow conception of sovereign immunity. See *Hess*, 513 U.S. at 52 (referring to "the concerns—the States' solvency and dignity—that underpin the Eleventh Amendment").[3]

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[3] The First Circuit placed excessive reliance on *Hess* while placing virtually none on the decisions noted in the text. Yet *Hess* is inapposite, it concerned *who* is protected by sovereign immunity, not the scope of *what* that immunity protects. *Hess* thus held that a bistate railway authorized by interstate compact enjoyed no Eleventh Amendment immunity because it was not an arm of either of its founding States. 513 U.S. at 52-53. The fact that the source of state funds is only one factor (not even the *exclusive* one) in the arm-of-the-state analysis suggests that the court of appeals erred in failing to acknowledge other immunity-related considerations. Here, of course, respondents sued petitioners in their respective capacities as state officials, Pet. App. 4a, so there is no question that this is a suit against a State, and no need for any arm-of-the-state analysis. See *Will* v. *Mich. Dep't of State Police*, 491 U.S. 58, 71 (1989) ("[A] suit against a state official in his or her official capacity is not a suit against the official but rather is a suit against the official's office. As such, it is no different from a suit against the State itself." (citation omitted)).

*Regents of the University of California* v. *Doe*, 519 U.S. 425 (1997), further undermines the First Circuit's exclusive focus on the state treasury. In that case, the Court rejected an argument "that the Eleventh Amendment does not apply to this litigation because any award of damages would be paid by [a third party], and therefore have no impact upon the treasury of the [State]." *Id.* at 431. This decision stands in stark contrast to what Chief Judge Lynch described as the First Circuit's proposed "exercise in forensic accounting." Pet. App. 66a (Lynch, J., dissenting from denial of rehearing en banc). Indeed, were it true that sovereign immunity depends solely on who cuts a check at the close of litigation, States could *extend* their sovereign immunity by indemnifying state officials in individual-capacity damage suits. Cf. *Scheuer* v. *Rhodes*, 416 U.S. 232, 237-238 (1974) (allowing such suits). But the federal courts have already rejected such machinations. See Richard H. Fallon, Jr. et al., *Hart and Wechsler's The Federal Courts and The Federal System* 999-1000 (5th ed. 2003); 13 Charles Alan Wright et al., *Federal Practice and Procedure* § 3524.2, at 282-283 (3d ed. 2008). Given that "a State may not confer Eleventh Amendment immunity on an entity or individual who would otherwise not enjoy that immunity simply by volunteering to satisfy judgments against the entity," *Doe*, 519 U.S. at 428, it stands to reason that a State does not lose its immunity when compelled by judicial decree to "volunteer" the funds of others.

b. The First Circuit is also incorrect that the States' constitutional immunity turns on the label attached to the public account that satisfies a

compensatory award. It is a distinction without a difference whether public funds are extracted from the general treasury or a designated account. This principle is apparent from the very order in this case: the reason the milk surcharge would not reach the public fisc is that the injunction itself directs the funds elsewhere in advance. This scheme is therefore materially indistinguishable (from the Commonwealth's perspective) from an order to distribute the same funds out of the general treasury—funded by the same taxpayers who contribute money by compulsion of the same law.

If a court cannot evade sovereign immunity by ordering an immediate lump-sum payment, there is no basis, as a legal or logical matter, for presuming a court could accomplish the identical result by ordering a future payment from a designated account created by the State's regulatory powers. This is precisely the kind of "forensic accounting" that has no obvious foundation in the constitutional structure. Pet. App. 66a (Lynch, J., dissenting from denial of rehearing en banc). Because the funds are properly characterized as public funds, the court of appeals' reasoning even fails on its own terms.

What matters in the end is the *incidence* of legal liability, see *Doe*, 519 U.S. at 431, *not* the technical source or location of any funds. Nor is there any doubt, contrary to the decision below, that the order established fault. The incidence of liability plainly fell on the Commonwealth—otherwise there would have been no basis for ordering a *non-liable* party to do much of anything, much less to order that party to invoke its sovereign powers at the behest of the federal judiciary.

3. The court of appeals also failed to recognize that sovereign immunity is implicated by a judicial decree compelling state officials to use the power of their office to regulate the citizenry—all with the aim of collecting public funds to satisfy a retrospective monetary award. Indeed, from the sovereign's vantage point, it is not clear exactly which of the following options is worse: an order extracting preexisting funds from the public treasury for retrospective relief, or an order compelling a State to invoke its regulatory machinery, in its sovereign capacity, to raise additional funds to cover the same retrospective payment. While respondents might not be taking funds directly from the State, the retrospective relief they seek (see Pet. 3 ("to recover the losses they have experienced" (quoting Second Am. Compl. ¶ 92, at 39))) still constitutes an order to satisfy an accrued liability that the Eleventh Amendment surely condemns. See, *e.g.*, *Papasan*, 478 U.S. at 279-281 (holding that Eleventh Amendment immunity bars suit for what was "in substance the award, as continuing income rather than as a lump sum, of an *accrued* monetary liability" (internal quotation marks omitted)).

Nor is this case anything like *Milliken*. That decision upheld an injunction ordering a State to pay millions of dollars toward a remedial education program for children suffering the lingering effects of racially segregated schools. 433 U.S. at 269, 288-290. Such relief was held to "fit[] squarely within the prospective-compliance exception reaffirmed by *Edelman*" and found necessary to cure *ongoing* violations of federal law. *Id.* at 289. Here, by contrast, plaintiffs sought an accrued monetary

liability—exactly the kind of relief *Milliken* itself rejected in explaining what it was *not* doing: "[T]here was no money award here in favor of [plaintiff] or any members of his class. This case simply does not involve individual citizens' conducting a raid on the state treasury for an *accrued* monetary liability." *Id.* at 290 n.22 (emphasis added).

That respondents "raid[ed]" the state armory instead of the state treasury is immaterial to the sovereign-immunity analysis. With their judicially imposed milk surcharge, respondents seek to commandeer the authority of state officials to obtain funds from Puerto Rican consumers. The milk surcharge does not differ from a tax in any meaningful way. Compare Pet. App. 64a-65a & n.11 (Lynch, J., dissenting from denial of rehearing en banc), with *id.* at 26a (panel opinion). The Court has held, in Eleventh Amendment cases involving frustrated state bond-holders, that "[a] private party cannot by judicial decree force a state officer to levy a tax." *Vann* v. *Kempthorne*, 534 F.3d 741, 753 (D.C. Cir. 2008) (describing this Court's jurisprudence). See *North Carolina* v. *Temple*, 134 U.S. 22, 30 (1890); *Hagood* v. *Southern*, 117 U.S. 52, 65-71 (1886); *Louisiana* v. *Jumel*, 107 U.S. 711, 720-723 (1883). In those cases, as here, private litigants sought to compel state officials to collect money from the public and transfer the funds elsewhere. This Court rejected such attempts as a result of sovereign

immunity; the First Circuit's failure to follow suit in this case warrants review—and reversal.[4]

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[4] Nor would respondents be correct to argue that subsequent events undermined the nineteenth-century bond cases. The 1908 decision in *Ex parte Young* did not overrule them, see, *e.g.*, *Worcester County Trust Co.* v. *Riley*, 302 U.S. 292, 296-297 (1937) (citing these cases alongside *Ex parte Young* as good law), and there was no occasion to overrule the Eleventh Amendment prohibition against judicial taxation in the school desegregation cases, which involved injunctions compelling *local*, not state, officials to levy taxes, see *Missouri* v. *Jenkins*, 495 U.S. 33, 55-56 & n.20 (1990); *Griffin* v. *County Sch. Bd.*, 377 U.S. 218, 232-233 (1964), cf. *Hibbs* v. *Winn*, 542 U.S. 88, 111 n.12 (2004) ("In school desegregation cases, as a last resort, federal courts have asserted authority to direct the imposition of, or increase in, *local* tax levies * * * ." (emphasis added)).

## CONCLUSION

The petition for a writ of certiorari should be granted, and the judgment of the court of appeals should be summarily reversed. Alternatively, the petition should be granted, and the case should be set for briefing and oral argument.

Respectfully submitted.

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